TMT sector game changers

A biannual report on new accounting and reporting trends—December 2019 edition

TMT Sector Game Changers is a biannual report highlighting new accounting and reporting trends affecting the Technology, Media and Telecommunications (TMT) industries, some of the most dynamic and competitive segments of today's economy. It's designed to help you stay informed and ahead of the curve amidst an ever-changing marketplace.

In this edition, we highlight TMT sector trends in M&A and capital markets, observations from this year's AICPA conference on SEC and PCAOB developments, a regulatory update on SEC developments related to LIBOR, key insights from the leasing standard adoption, data trust insights, and SEC comment letter trends.

TMT deals, IPOs, and debt offerings

Following a very hot second quarter of the year, US IPO markets cooled off slightly in Q3'19, as global economic uncertainty and market volatility increased. The US IPO market remains buoyant and represents a very attractive platform for valuation-setting, capital–raising, acquisition currency, employee retention and investor exits.

IPO activity in the third quarter slowed, with 11 IPOs in the TMT sector, compared to 22 in the prior quarter, as backlog from the government shutdown resolved. Investors became less eager to invest in fast-growing, but cash-burning tech IPOs, as they saw the lackluster performance of recent unprofitable tech IPOs. In line with six of the last seven quarters, TMT once again led in proceeds raised with 11 IPOs raising $4.1 billion in Q3 2019, because of continued investor interest in scalable software companies. TMT IPOs in Q3 2019 were highlighted by both DouYu International Holdings Ltd. ($0.8B raised) and Datadog, Inc. ($0.7B raised).

Tech deals value came in significantly lower compared to the prior four quarters, as potential buyers were deterred by political regulatory, and macroeconomic uncertainties. Q3 2019 deal activity continues to highlight the strength in software, especially companies in the software-as-a-service and security subsectors. While total deal value in Q3 2019 declined 46% from the second quarter, overall deal value for 2019 is up 37% compared to 2018, driven by 9 mega deals for $138B, highlighted by Broadcom's acquisition of Symantec's Enterprise Security division, VMware's acquisitions of Pivotal Software and Carbon Black, and Salesforce's acquisition of Clicksoftware. While the expectation of a recession will likely deter deal activity in the near term, we expect corporate tech buyers to continue to drive the M&A market in a downturn as lower valuations coupled with significant availability of capital will spur deal activity from savvy buyers.

Media and Telecommunications Q3 2019 deal volumes rebounded after a slow start to the first half of the year, with an increase in announced deal volume over the prior quarter of 16%, highlighted by the announcement of the long-rumored CBS and Viacom merger and Dish's announced acquisition of Sprint's prepaid and spectrum assets. Major players are now turning towards integrating recent acquisitions and monetizing their strengthened content libraries, ahead of the impending streaming wars. Looking ahead, we expect to see M&A trend towards OTT-driven content and data and AI-driven deals, while a consolidation of digital publishing platforms begins to take shape.

Read more from PwC at PwC Q3 2019 Capital Markets Watch , US Technology Deals Insights Q3 2019 , and US Media and Telecommunications Deals Insights Q3 2019

AICPA conference on SEC and PCAOB developments

The 2019 AICPA National Conference on Current SEC and PCAOB Developments took place December 9–11, 2019. The conference featured representatives from regulatory and standard-setting bodies, along with auditors, preparers, securities counsel, and industry experts. Consistent with prior years, the theme of the conference focused on collaboration and transparency. Topics discussed at the conference included: observations on registrants' implementations of the Revenue and Leases accounting standards including an analysis of factors that contributed to successful implementations. Additionally, conference topics included observations relative to monitoring of implementation of the Current Expected Credit Losses (CECL).

The Office of the Chief Accountant has been actively engaged in consultation questions about the leases standard, including those related to the scope of the standard, transition, and certain lessee and lessor costs. Additional topics discussed included the ongoing FASB projects on the standard-setting agenda including subsequent accounting for goodwill, distinguishing liabilities from equity, and reference rate (LIBOR) reform.

Listen to our podcast for highlights of 2019 AICPA Conference on Current SEC and PCAOB Developments for additional details on PwC's point of view of the conference.

Regulatory update—SEC developments related to LIBOR

The London Interbank Offer Rate (LIBOR) is a measure of the average interest rate at which major global banks borrow from one another and is used as a reference rate for various commercial and financial contracts. Currently, it is expected that LIBOR will be discontinued after 2021, which could give rise to significant operational and financial reporting implications as companies work to identify contracts exposed to LIBOR and paths to transition to an alternative reference rate.

On July 12, 2019, the SEC staff issued a statement on LIBOR transition. The statement reiterated that the expected discontinuation of LIBOR could have a significant impact on financial markets and may present a material risk for certain market participants. The staff indicated that it is actively monitoring the extent to which registrants are identifying and addressing risks associated with LIBOR transition. The staff encouraged market participants to begin the process of identifying existing contracts that extend past 2021 to determine their exposure to LIBOR and identify whether their existing contracts address circumstances where LIBOR is no longer available. As part of managing the transition, the staff also encouraged companies to identify what alternative reference rate might replace LIBOR in existing contracts.

In addition to providing practical guidance regarding the expected transition from LIBOR, the statement also identified areas of disclosure that the SEC's Division of Corporation Finance will be monitoring in future filings with the SEC. These areas include: The status of efforts regarding transition and significant areas yet to be addressed, any identified material exposures to LIBOR for which the impacts are not yet known or cannot be reasonably estimated, the information used by management and the Board of Directors to assess and monitor transition, including qualitative and quantitative disclosures as applicable

Leasing adoption

What are TMT companies saying about their adoption journey?

The results of our 2019 lease accounting survey are in, and while the deferral of ASC 842 for private companies may provide some relief, there are many opportunities for private companies to learn from public company adoption in 2019. Our recent survey also provides insights into what “Day 2” challenges public companies are continuing to work through.

Systems and automations

Of the 72% that have implemented new or modified existing systems to account for leases under the new standard, 31% are still exploring system enhancements or alternatives. Also, 70% cited manual work-arounds required for lease reporting following their initial system implementation, with much focus on improved reporting to support the enhanced disclosure requirements.

For private companies, **32%** expect to implement a new system and **60%** are planning to use desktop applications (i.e. spreadsheets), while 50% of public companies will use new systems and only **35%** are using existing desktop applications.

Budgeting and resources

84% of private companies have 4 or less people on team and **81%** expect to spend under **$250k**

Only **51%** of public companies had implementation teams of 4 or less, while **35%** have over 7 people on the team and **40%** of public companies spent in excess of **$500k**

Status of implementation

Though half of private companies have not changed their implementation timeline as a result of the deferral, **34%** of companies have prioritized other projects as a result of the deferral.

55% of private companies have not yet started or are in-process of assessing the impact of the standard

39% of public company respondents across all industries, continue to develop, remediate, or design and implement key controls over the new leasing standard in the fourth quarter of their year of adopting

Learn from over 900 respondents to our survey, with information specific to the TMT sector by exploring the results using our accounting change survey data explorer.

Public company challenges—Day 2

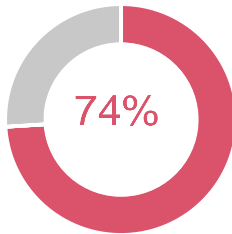
Subsequent to recording the impact upon adoption, “Day 2” accounting has also presented challenges to public entities. Seventy-seven percent of public company respondents are facing challenges with automating new lease reporting. Ongoing data capture and strengthening of key controls implemented with the adoption also rank as top issues reported in our survey.

Private company challenges—Implementation

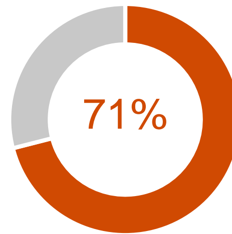
Top implementation challenges from private company respondents include completeness of the lease population, identification of embedded leases, and data extraction.

Implementation challenges

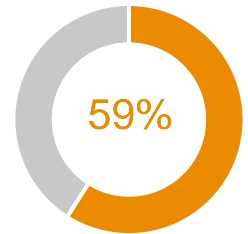
Non–public Company responses % choosing “Very” or “Somewhat” difficult



Ensuring completeness of lease population



Identifying embedded leases



Data abstraction

Source: PwC’s 2019 lease accounting survey

Private companies are likely to benefit from understanding the key adoption challenges experienced by their public company peers which have included themes such as completeness of the lease population, identification of embedded leases, and completeness and accuracy of data extraction. Public companies are facing their own challenges with "Day 2" accounting including both automating key lease processes and internal controls related to the leasing process.

Read more from PwC: Refer to CFOdirect.com to take a deeper dive into the results of the ASC 842 implementation.

Cloud computing arrangements: Customer accounting for implementation cost

Many companies are moving data, applications, and platforms to the cloud. Migration from a traditional IT model to the cloud may create substantial business benefits because companies may be able to reduce capital expense outlays while maintaining a more flexible IT environment. As companies move to a cloud-based environment, software products that have traditionally been installed locally on a customer's server are now often hosted on a vendor's server and accessed by the customer remotely. These arrangements are typically referred to as cloud computing arrangements (CCAs). Companies should consider the financial reporting implications as well as broader tax and IT considerations as a result of IT transformation.

Key Takeaway: The presentation requirements could impact key metrics such as EBITDA as the deferral of CCA costs will not be included within depreciation or amortization expense. Companies should also consider the related impact to their budgeting and financial planning processes that may drive earnings guidance.

The new guidance

To reduce diversity in practice, the FASB issued new guidance in August 2018 that requires companies to account for implementation costs related to CCAs using the same accounting rules as software that is licensed or developed for internal use. As a result of this new guidance, many implementation costs will now be deferred and amortized over the term of the CCA.

The new cloud computing guidance requires companies to present implementation costs related to a CCA in the same financial statement line items as the CCA service fees, resulting in key differences from the presentation of costs related to licensed software:

Financial Statement	Licensed software	CCA Arrangement
Balance Sheet	Intangible or Fixed asset	Prepaid or Other Assets
Income Statement	Depreciation or Amortization	Operating Expenses
Statement of Cash Flows	Investing Activity	Operating Activity

Key tips and observations:

As companies prepare to adopt the new CCA standard, a number of operational and practical challenges may arise. Based on our experience, the following are common areas of challenge:

- Determining what arrangements fall under the scope of this guidance (e.g. moving existing on-premise software to cloud versus implementation of a cloud-based solution).
- Determining which activities qualify for capitalization versus expense treatment.
- Evaluating activities performed by third-party service providers to identify or estimate the portion of costs that should be capitalized.
- Evaluating implementation costs for each significant component or instance of a CCA, which may have different implementation timing and impairment considerations.
- Exercising judgment to determine whether the amortization period should include renewal periods.
- Assessing downstream implications to areas outside of accounting, such as IT, financial planning, and income taxes.
- Establishing Company-wide policies and guidelines for applying the new guidance.
- Designing and implementing new processes and controls to: identify, track and evaluate costs for capitalization, determine the amortization period, assess assets for impairment, and prepare new disclosures.

Timing

This new guidance is effective in 2020 for public business entities. For all other entities, this guidance is effective for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. The new cloud computing guidance is not optional–that means companies are required to track implementation costs related to a CCA and evaluate whether those costs should be capitalized.

Read more from PwC: Refer to CFOdirect.com for the publication: Moving to the cloud? Business considerations for the new cloud computing accounting standard to find out more about the broader business implications that accompany a cloud transformation.

You can also hear more about the broader implications of the new CCA standard by viewing our animated video: Using cloud computing? Consider the financial reporting rules and broader business impacts.

Data trust pacesetters

A small group of companies are leading the way in building trust in data.

If your company does not yet have a formal process for valuing its data assets, you are in the minority. Seventy-two percent of more than 3,500 respondents to PwC's Digital Trust Insights survey said their organization already has one.

The survey respondents' primary ambitions for investing in data is to bring the highest value in the form of data-enabled products and services (41%), followed by a desire to be the most efficiently run organization in their industry (35%).

The biggest challenges to their ambitions result from the lack of confidence in the quality of their data and their ability to safeguard that data by preventing data theft and leakage, protecting the integrity of data, and managing privacy risks. Only 25% of consumers believe companies handle their data responsibly.

That's why it's time to shift to a data trust strategy, not just a data strategy. Of the survey respondents who have a formal process for assigning value to their data, 37% involve the data privacy team consistently in the process. These companies are the data trust pacesetters.

Pacesetters know that possession and use of data create responsibilities, which in turn affect the data's value. Many regulations now specify the way data needs to be handled (which adds compliance costs), the limits on the use of data (which reduces commercialization potential), and the consequences of losing data (which increases risks and costs).

Our analysis shows the pacesetters stand out in five distinct areas. They offer a guide for any company looking to improve its ability to extract value from its data in a secure and ethical way.

Pacesetters:

1. Consistently involve the data privacy team when valuing data. By incorporating risk management into their data development efforts, pacesetters can identify potential problems and help protect against them before catastrophe strikes.

2. Routinely value data. Pacesetters not only effectively assign value to data, they also establish processes to ensure that value is applied consistently across data sets.

3. Adopt leading practices in ethical use of data. Pacesetters have defined responsibilities across the organization to ensure data's ethical use. As part of this practice, they embrace technology to power/direct data protection, management and governance.

4. Embrace leading practices in data engineering. Pacesetters create design tools that incorporate security and privacy into their systems, products and services. They create comprehensive data maps for risk assessments and controls testing.

5. Form a collaborative team with the authority to act. Data pacesetters build cross-functional data governance teams to understand the data and develop processes for using it ethically.

Read more from PwC at Five traits of data trust pacesetters.

SEC comment letter trends

The SEC Division of Corporate Finance's filing review process is a key function utilized by the SEC staff to monitor critical accounting and disclosure decisions applied by registrants. Our analysis of SEC comment letters identifies the frequency of topical areas addressed by the SEC staff and how their focus areas have changed over time. Read more on SEC comment letter trends for Technology, media, and telecommunications companies where we provide our insights on the nature of the SEC staff comments, sample text from the comments and links to where you can learn more about the accounting and disclosure requirements addressed in each topical area.

	Current Period (10/1/2018 – 9/30/2019)*	Relative change in number of letters compared to the prior period*
1	Revenue recognition	↑
2	Non-GAAP measures	↔
3	Segment reporting	↓
4	Fair value measurement	↓
5	Management's discussion and analysis	↓
6	Terrorist nation sponsor reporting	↓
7	Income taxes	↔
8	Disclosure controls and ICFR	↔
9	Goodwill and other intangibles	↓
10	Accounting changes and error corrections	↔

* This analysis was performed based on topical areas assigned by research firm Audit Analytics for comment letters publicly issued in the 12 months ended September 30, 2019 ("Current Period") and the 12 months ended September 30, 2018 ("Prior Period") in relation to Form 10-K and Form 10-Q filings. Total comment letters evaluated during the Current Period and Prior Period were approximately 230 and 220, respectively.

Legend

The relative number of comment letters has increased.

The relative number of comment letters has decreased.

The relative number of comment letters has not changed significantly.

Key observations from comment letters

Related to revenue recognition comment letter trends, topics most frequently addressed in the SEC staff's comments include: the nature of performance obligations and why goods or services are distinct, how a company estimates variable consideration, the determination of appropriate costs to capitalize and the related amortization period, gross versus net presentation judgments, and disaggregation of revenue disclosures.

Non-GAAP financial measure result in frequent comments regarding compliance with Item 10(e) of Regulation S-K, sometimes resulting in requests to remove or substantially modify non-GAAP metrics. Focus areas include: presentation with equal or greater prominence or reconciliation to the most directly comparable GAAP financial measure, and disclosure of why management believes the non-GAAP presentation provides useful information to investors.

Fair value measurements often require the application of significant judgment. The SEC staff has focused on the quality of disclosure around those significant judgments and estimates. Key areas of focus include: the valuations techniques and key inputs used to determine the fair value, the quantitative information provided for significant unobservable inputs used in Level 3 fair value measurements, and the sufficiency of disclosures related to non-recurring fair value measurements, such as impairments.

Are you responding to a comment letter? Read our best practices on The Comment Letter Process.

Accounting standard update

ASU No.	Standard Name	Effective Date**	PwC Resources
ASU 2016-13 ASU 2018-19	Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	Fiscal years beginning after December 15, 2019 for SEC filers (December 15, 2020 for all other public business entities), including interim periods within those fiscal years*	Accounting guide In the loop
ASU 2017-04	Intangibles—Goodwill and Other (Topic 350)	SEC filers: Annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019* Non-SEC filers: Annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2020*	Accounting guide
ASU 2018-13	Fair Value Measurement (Topic 820) Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement	Fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019*	Accounting guide
ASU 2018-15	Intangibles—Goodwill and Other— Internal-Use Software (Subtopic 350-40) Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract	Fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019*	In depth
ASU 2018-17	Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities	Fiscal years beginning after December 15, 2019, and interim periods within those fiscal years*	In brief

About PwC's TMT industry practice

PwC's TMT practice strives to help business leaders in the Technology, Media and Telecommunications industries manage their complex businesses and capitalize on new windows of opportunity. With offices in 158 countries and more than 250,000 people, we help organizations and individuals create the value they're looking for by delivering quality in assurance, tax, and advisory services. Visit our website at: www.pwc.com/us/tmt

Let talk

For a deeper discussion on the content included in this edition of TMT Sector Game Changers or other challenges, please reach out to any of our TMT leaders to discuss. We're here to help.

Mark McCaffrey
US TMT Industry Leader
mark.mccaffrey@pwc.com

Kevin Healy
US TMT Assurance Leader
kevin.healy@pwc.com

Contributors: Scott Morency, Chris Rhodes, Kris Scribner, Jay Cline, Ryan Spencer, Joseph Nocera, Mir Kashifuddin, Sean Joyce, Shawn Connors, and Brandon Campbell Jr.

© 2019 PwC. All rights reserved. PwC refers to the US member firm or one of its subsidiaries or affiliates, and may sometimes refer to the PwC network. Each member firm is a separate legal entity. Please see www.pwc.com/structure for further details.