



Accounting Roundup

Year in Review — 2006



The purpose of this publication is to briefly describe key regulatory and professional developments that have recently occurred in the field of accounting and to provide links to locations where additional information can be found on each topic. Readers seeking additional information about a topic should review the information referred to in the hyperlinks and not rely solely on the descriptions included in this communication.

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To our clients, colleagues, and other friends,

Welcome to the 2006 edition of *Accounting Roundup Year in Review*. In 2006, standard setters and regulators were busy once again, issuing guidance on the following topics:

- Fair value measurements.
- Pensions and other postretirement benefit obligations.
- Uncertain tax positions.
- Amendments to FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*.
- Quantifying misstatements.

This issue of *Accounting Roundup Year in Review* summarizes these topics and other final guidance issued in 2006; proposed guidance, such as Exposure Drafts and Invitations to Comment, is not included. Please refer to our 2006 monthly and quarterly issues of *Accounting Roundup* for more information about these documents and about the deadlines for related comment letters.

For more information about a topic, click one of the blue links, which are indicated by the  symbol. The links give access to useful resources such as the Web sites of the relevant standard setters, including the FASB, GASB, SEC, PCAOB, AICPA, and IASB.

We predict that 2007 will be another busy year; the FASB has added a project to its agenda on lease accounting, and final guidance is expected to be issued on the following topics:

- Business combinations and noncontrolling interests.
- Fair value options.
- Derivatives disclosures.
- Financial guarantee insurance.

We encourage you to keep up to date on the actions of the regulators and standard setters during 2007 through our *Accounting Roundup* series, *EITF Roundup* series, *Heads Up* articles, and Dbriefs webcasts. We hope that *Accounting Roundup Year in Review* will prove valuable for financial reporting purposes. We welcome your feedback. Please send questions and comments to accountingstandards@deloitte.com.

Sincerely,

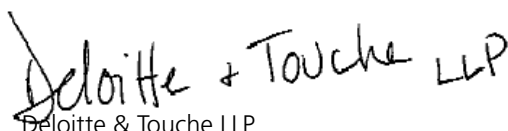

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Fair Value Measurements

Current accounting pronouncements on fair value focus on **what** to measure at fair value rather than **how** to measure fair value; such GAAP defines fair value inconsistently and contain limited guidance on its application. Statement 157 addresses this situation: it is a **“one-stop shopping” source that provides a single definition of fair value as well as measurement guidance**. Though it does not introduce any new measurement requirements, Statement 157 does add important disclosure requirements. We summarize the new Statement below and provide a link to more information.

FASB Issues Statement No. 157, *Fair Value Measurements*

AFFECTS: All companies that apply fair value measurements.

SUMMARY: Statement 157 provides a single definition of fair value, along with a framework for measuring it, and requires additional disclosure about using fair value to measure assets and liabilities. The Statement emphasizes that fair value measurement is market-based, not entity-specific, and establishes a fair value hierarchy in which the highest priority is quoted prices in active markets. Under Statement 157, fair value measurements are disclosed according to their level within this hierarchy. While the Statement does not add any new fair value measurements, it does change current practice in the following ways:

- It requires entities to include their own credit standing when measuring their liabilities.
- It modifies the transaction price presumption.¹
- It prohibits broker-dealers and investment companies from using block discounts when valuing large blocks of securities.
- It requires entities to adjust the value of restricted stock for the effect of the restriction even if the restriction lapses within one year.

EFFECTIVE: For financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Earlier application is encouraged, provided that no financial statements have yet been issued within that fiscal year by the reporting entity.

TRANSITION: Statement 157 shall be applied prospectively as of the beginning of the fiscal year in which the Statement is initially applied, other than the exceptions described in paragraphs 37(a)–37(c). Those exceptions require retrospective application as of the beginning of the fiscal year in which the Statement is initially applied.

OTHER RESOURCES: Deloitte & Touche's [Heads Up](#) on Statement 157.

Employee and Director Compensation

Standard setters and regulators focused on various areas of employer and director compensation during 2006. In late 2006, the FASB issued Statement 158, which requires that most public companies **fully recognize an asset or liability for the overfunded or underfunded status of their benefit plans** in financial statements for years ending after December 15, 2006. In addition, the SEC issued rules designed to provide greater transparency in executive and director compensation, as well as further guidance on the appropriate application of the stock option accounting literature (primarily Opinion 25). Furthermore, Statement 123(R), issued in 2004, continued to be a topic of discussion throughout 2006, with the FASB responding to continuing requests for implementation guidance by issuing a series of FSPs on the valuation of share-based payment awards and other issues. We summarize Statement 158, the FSPs related to 123(R), the SEC's compensation disclosure rules, and other literature issued throughout the year that addresses employee and director compensation.

FASB Issues Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106, and 132(R)*

AFFECTS: All companies that sponsor a postretirement benefit plan.

SUMMARY: By amending Statements 87 and 106, Statement 158 addresses certain deficiencies in the original pension

¹ Statement 157 nullified footnote 3 of EITF Issue No. 02-3, “Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities,” and paragraph 4(d) of FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*, which added paragraph 16A of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*.

accounting guidance. Most important, Statement 158 increases the transparency of an entity's financial statements. The Statement requires an entity that sponsors a postretirement benefit plan(s) to recognize fully, as an asset or liability, the overfunded or underfunded status of this plan in its year-end balance sheet (for calendar year-end companies with publicly traded equity securities, this provision is required in the 2006 year-end balance sheet). The funded status is measured as the difference between the fair value of the plan's assets and its benefit obligation. The benefit obligation's measurement basis is the projected benefit obligation for pension plans and the accumulated postretirement obligation for other postretirement benefit plans.

In addition, Statement 158 requires that an entity measure its plan assets and benefit obligations as of its year-end balance sheet date. Currently, an entity is permitted to choose a measurement date of up to three months prior to its year end. Paragraph 5 of Statement 158 cites two exceptions to the measurement date provision. Those two situations, and the way in which the measurement date is affected, are as follows:

- When a subsidiary is the plan sponsor and a different fiscal period than that of its parent is used to consolidate the subsidiary, the parent should measure the subsidiary's postretirement benefit plan assets and benefit obligations as of the same date used to consolidate the subsidiary.
- When the plan is sponsored by an equity method investee and the financial statements of the equity method investee are not available in time for the investor to currently apply the equity method, the investor should measure the investee's plan assets and benefit obligations as of the same date of the investee's financial statements used to apply the equity method.

Statement 158 does not address the measurement and recognition issues related to the changes in the fair value of plan assets and benefit obligations. These and other issues will be the primary focus of a multiyear Phase II project. Accordingly, Statement 158 does not affect an entity's computation of its benefit expense recognized in the income statement.

EFFECTIVE: The provisions and their effective dates are as follows:

- Recognition of an asset or a liability related to the funded status of a plan and related disclosures:
 - For entities with publicly traded equity securities, effective for fiscal years ending after December 15, 2006.
 - For all other entities, effective for fiscal years ending after June 15, 2007.
- Measurement of the entity's year-end balance sheet date:
 - For all entities, effective for fiscal years ending after December 15, 2008.
- Early adoption is permitted.

TRANSITION: The Statement requires prospective application.

OTHER RESOURCES: Deloitte & Touche's [Heads Up](#) on Statement 158.

FASB Issues Final FSPs Related to Statement 123(R)

Final FSP FAS 123(R)-5

AFFECTS: Entities that apply, or should apply, Statement 123(R).

SUMMARY: FSP FAS 123(R)-5 addresses whether a modification of an instrument in connection with an equity restructuring should be considered a modification for purposes of applying FSP FAS 123(R)-1. This FSP states that no change in the recognition or the measurement (due to a change in classification as a result of a modification solely to reflect an equity restructuring that occurs when the holders are no longer employees) of the instruments will result if two conditions are met: (1) there is no increase in fair value of the award (or the ratio of intrinsic value to the exercise price of the award is preserved — that is, the holder is made whole) or the antidilution provision is not added to the terms of the award in contemplation of an equity restructuring, and (2) all holders of the same class of equity instruments (for example, stock options) are treated in the same manner. Other modifications that take place when the holder is no longer an employee shall be subject to the modification guidance in paragraph A232 of

Statement 123(R).

EFFECTIVE: The FSP shall be applied in the first reporting period beginning after October 10, 2006. Early application is permitted in periods for which financial statements have not yet been issued.

TRANSITION: If an entity applied Statement 123(R) in a manner consistent with the provisions of this FSP, then continued application is required prospectively. Otherwise, an entity should apply the provisions of this FSP retrospectively.

Final FSP FAS 123(R)-6

AFFECTS: Entities that apply, or should apply, Statement 123(R).

SUMMARY: FSP FAS 123(R)-6 addresses certain technical corrections of Statement 123(R). The amendments exempt nonpublic entities from disclosing the aggregate intrinsic value of fully vested share options (or share units) expected to vest at the date of the latest statement of financial position. This FSP also revises the definition of “short-term inducement” to exclude an offer to settle an award. In addition, it revises two illustrations to comply with paragraph 42 in Statement 123(R) and to clarify reversal dates for modifications.

EFFECTIVE: For the first reporting period beginning after October 20, 2006. Early application is permitted in periods for which financial statements have not yet been issued.

TRANSITION: If an entity applied Statement 123(R) in a manner consistent with the provisions of this FSP, then continued application is required prospectively. Otherwise, an entity should apply the provisions of this FSP retrospectively.

FASB Staff Position No. FAS 123(R)-4, “Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement Upon the Occurrence of a Contingent Event”

AFFECTS: Companies that issue options or similar instruments as employee compensation.

SUMMARY: An award of options or similar instruments that meets the criteria for equity classification, except for containing a cash settlement feature that requires the entity to settle the award in cash only if a contingent event occurs that is outside the employee’s control, should be classified as a liability only when the event is “probable of occurring.” If it is not probable that the contingent event will occur, equity classification is required. However, public companies will still be required to present equity-classified options as “mezzanine equity” outside of permanent equity, in accordance with ASR 268 (FRR Section 103) and Topic D-98.

EFFECTIVE: Upon initial adoption of Statement 123(R). For an entity that adopted Statement 123(R) before February 3, 2006, FSP 123(R)-4 is effective for the first reporting period beginning after February 3, 2006.

TRANSITION: Retrospective application of the FSP to prior periods is required if, in initially applying Statement 123(R), an entity treated options or similar instruments that allow for cash settlement upon the occurrence of a contingent event in a manner inconsistent with the guidance in the FSP.

OTHER RESOURCES: [Subscribe](#) to the Deloitte & Touche *Roadmap* series.

EITF Issue No. 06-4, “Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements”

AFFECTS: Entities (most notably community banks) with endorsement split-dollar life insurance arrangements that provide employees with a specified benefit not limited to the employee’s active service period, including certain company-owned life insurance (COLI) or bank-owned life insurance (BOLI) policies.

SUMMARY: An employer should recognize a liability for future benefits on the basis of the substantive agreement with the employee. In reaching the consensus in Issue 06-4, the Task Force concluded that entering into an

endorsement split-dollar life insurance arrangement does not qualify as a settlement under Statement 106. The liability should be recognized in accordance with Statement 106 — if deemed part of a plan — or Opinion 12.

The Task Force acknowledged that the substantive agreement often constitutes an employer's commitment to keep an insurance policy in effect during the employee's retirement period. However, determining the substance of an arrangement involves consideration of all available evidence, including, but not limited to, the explicit written terms of the arrangement, communications between the employer and employee, and the identity of the primary obligor of the benefit (i.e., the employer or the insurance company).

EFFECTIVE: For fiscal years beginning after December 15, 2007, with earlier application permitted.

TRANSITION: Entities should recognize the effects of applying the consensus through either (1) a change in accounting principle through a cumulative-effect adjustment to retained earnings or to other components of equity or net assets as of the beginning of the year of adoption or (2) a change in accounting principle through retrospective application to all prior periods.

EITF Issue No. 06-2, "Accounting for Sabbatical Leave and Other Similar Benefits Pursuant to FASB Statement No. 43, *Accounting for Compensated Absences*"

AFFECTS: Entities that provide employees with a compensated absence under sabbatical or other similar benefit arrangements.

SUMMARY: Issue 06-2 addresses whether an employer should accrue a liability for an employee's right to a compensated absence under a sabbatical or other similar benefit arrangement that (a) requires the completion of a minimum service period and (b) does not increase with additional years of service.

Paragraph 6 of Statement 43 provides guidance on this, stating that a future obligation should be accrued as a liability if the "obligation relates to rights that vest or accumulate." The Task Force concluded that the **employee's right does accumulate**; therefore, it should be accrued over the required service period.

EFFECTIVE: For reporting periods beginning after December 15, 2006.

TRANSITION: The effects of applying the consensus should be recognized as a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption. Retrospective application is allowed but not required. Entities should disclose the cumulative effect of the change on retained earnings. Early adoption is permitted as of the beginning of an entity's fiscal year, provided that the entity has not yet issued financial statements, including interim financial statements, for any period of that fiscal year.

OTHER RESOURCES: Deloitte & Touche's [June 2006 EITF Roundup](#).

SEC Finalizes Disclosure Requirements for Executive and Director Compensation

AFFECTS: SEC registrants and their auditors.

SUMMARY: Final Rule Release 33-8732A increases the disclosure requirements of total compensation for the principal executive officer, the principal financial officer, and up to three of the other most highly paid officers. It also expands compensation disclosures for directors by requiring that all compensation to each director be disclosed in a separate summary compensation table. The amendments are intended to provide a clearer and more complete picture of the total compensation of such persons.

The Final Rule requires that disclosures combine a tabular presentation with improved narrative. Disclosures should begin with an overview entitled "Compensation Discussion and Analysis," which includes material factors in determining compensation policies and decisions reflected in the data in the tables. This discussion should cover the design and objectives of the company's compensation program; how the elements are calculated and paid; and a company's policies, programs, and practices regarding the awarding of stock options. Furthermore, in the discussion section a company should also disclose whether it has, or intends to have, a plan or practice of setting (1) the exercise price of stock options at other than the market price at the grant date or (2) grant dates in coordination with the release of nonpublic information.

After the Compensation Discussion and Analysis, companies should make the following tabular

disclosures:

- A summary compensation table that presents compensation paid or currently deferred, consisting of current earnings or awards that are part of a plan. Certain data in this table will be supplemented by additional tabular disclosures.
- Holdings of equity-related interests that relate to compensation or that are potential sources of future gains, which potentially includes three tables describing the following: grants of plan-based awards, outstanding equity awards at fiscal year end, and option exercises and stock vested.
- Retirement and other postemployment compensation, which includes tables of pension benefits and a nonqualified deferred compensation.

EFFECTIVE: The new requirements are effective in Forms 8-K for triggering events that occur on or after November 7, 2006; in Forms 10-K and 10-KSB for fiscal years ending on or after December 15, 2006; and in registration and proxy/information statements filed after December 15, 2006.

OTHER RESOURCES: Deloitte & Touche's *Heads Up* on the Final Rule.

Amendment to Executive Compensation Disclosure Rules

AFFECTS: Public companies and their auditors.

SUMMARY: The SEC issued Interim Final Rules Release 33-8765, which amends the disclosure requirements for executive and director compensation. Under the amended rules:

- The summary compensation table and the director compensation table will include the compensation cost of stock awards and option awards over the requisite service period, as defined in Statement 123(R), instead of the aggregate grant date fair value of awards computed in accordance with Statement 123(R).
- The grants of plan-based awards table will include the following information computed in accordance with Statement 123(R):
 - A column showing, on a grant-by-grant basis, the full grant date fair value of awards.
 - The incremental fair value of repriced or materially modified options, stock appreciation rights, and similar optionlike instruments, computed as of the repricing or modification date.

EFFECTIVE: The amendments are effective December 29, 2006. However, because these are interim final rules, the SEC has indicated that it will consider constituents' comments provided by January 29, 2007, so that it can make any necessary revisions.

OCA Expresses Its Views on the Appropriate Application of the Stock Option Accounting Literature

AFFECTS: SEC registrants that grant stock options.

SUMMARY: Companies' past practices in granting stock options have precipitated restatements of financial statements. Responding to these recent restatements, the Office of the Chief Accountant (OCA) of the SEC has issued a letter outlining its views on the appropriate application of the relevant accounting guidance, including a company's determination of the measurement date of past stock option awards under Opinion 25. The OCA staff notes that as a result of differences in the accounting standards, the views expressed in the letter do not necessarily represent the staff's views on determining grant date and measurement date under Statement 123(R).

The letter is divided into individual sections containing a description of, and the OCA staff's views on, each issue. The most significant topics discussed are:

- Dating option awards to predate the actual award date.
- Option grants with administrative delays.
- Validity of prior grants.
- Uncertainty about individual award recipients.
- Exercise price set by reference to a future market price.
- Grants prior to the commencement of employment.
- Missing or incomplete documentation of option granting activities.

- Granting option awards before the release of new information,
- Changes to option grants owing to the release of new information.
- Income tax benefits related to options.

OTHER RESOURCES: Deloitte & Touche's *Heads Up* on the SEC letter.

SEC Sample Letter Provides Guidance on Stock Option Grants Restatements

AFFECTS: Public companies planning to restate financial statements for errors in accounting for stock option grants.

SUMMARY: Several public companies, preparing to restate financial statements for errors in accounting for stock option grants, have asked the SEC's Division of Corporation Finance for filing guidance. In December 2006, the Division of Corporation Finance responded with a sample letter that provides registrants with such guidance.

The sample letter indicates that a restatement of financial statements for errors in accounting for stock option grants may affect several years. As a result, it may be overly burdensome for a company to amend all previously filed financial statements. In addition, the filing of multiple amendments could impair a financial statement user's ability to understand the restatement's impact.

The staff of the Division of Corporation Finance indicates that it will not raise further comment regarding a registrant's need to amend prior Exchange Act filings to restate financial statements and related MD&A if that registrant amends its most recent Form 10-K and **includes in that amendment the comprehensive disclosures outlined in the letter**. If a registrant's next Form 10-K is due to be filed within two weeks of the Form 10-K amendment that it would file in response to this guidance, the staff will not comment on the registrant's need to amend or file prior Exchange Act filings to restate financial statements and related MD&A if that registrant **includes the comprehensive disclosures outlined in the letter** in the next Form 10-K — rather than in an amendment to its most recent Form 10-K.

PCAOB Issues Audit Practice Alert on Stock Option Grants

AFFECTS: Auditors of companies that issue stock options.

SUMMARY: Audit Practice Alert (APA) 1 focuses on so-called discount or in-the-money options (i.e., the strike price is below the market price on the measurement date). These are more valuable than typical options that, on the measurement date, have a zero intrinsic value (a technical option term meaning the excess of the current market price over the exercise price). At issue are situations in which an issuer fails to properly consider the impact of the discount on the original accounting.

The APA points to a range of practices, not all-inclusive, that could result in discounting. In addition, the APA warns that auditors planning or performing an audit should be alert to risks arising from an issuer's improper accounting for stock option grants and should perform appropriate procedures in response to these risks, including acquiring sufficient information to assess their nature and potential magnitude. Furthermore, the APA addresses auditor involvement in registration statements and the effects of option-related matters on previous opinions. Finally, the APA recommends consideration of other appropriate guidance on auditing and related matters.

OTHER RESOURCES: Deloitte and Touche's *Heads Up* on the APA. The *Heads Up* provides specific examples of the APA's applicability.

Q&As Issued on Auditing the Fair Value of Share Options Granted to Employees

AFFECTS: Auditors of companies that estimate the fair value of stock options granted to employees pursuant to Statement 123(R).

SUMMARY: To help auditors implement the PCAOB's existing auditing standards when auditing the fair value of share options granted to employees, the PCAOB has issued staff Q&As. The document poses several questions and provides the staff's opinions on auditing financial statements in which a company has granted share options to employees that must be accounted for as compensation cost in conformity with Statement 123(R). The Q&As highlight risk factors to be aware of, address the auditor's consideration of the process for developing a fair value estimate, highlight significant assumptions used in options pricing models, and discuss the role of specialists in fair value measurements.

AICPA Employee Stock Option Financial Reporting Alert

AFFECTS: Companies that issue share-based payments and their auditors.

SUMMARY: The Alert provides an overview of FASB Statement No. 123(R) and SAB 107. Topics include:

- Employee stock options.
- The controversy surrounding stock option expensing.
- The likely effects of Statement 123(R).
- The value of a stock option.
- How to minimize stock option expense.

Financial Instruments and Derivatives

Financial instruments and derivatives continue to be a hot topic in the accounting field. As new and increasingly complex financial instruments are created in the marketplace, constituents of the FASB consistently request that standard setters provide guidance on how to account for such instruments. Although Statements 155 and 156 discuss various types of derivatives, they also highlight the use of fair value. Statement 155 is a stopgap until the issuance of another final Statement, *The Fair Value Option for Financial Assets and Financial Liabilities*, which the FASB plans to issue in early 2007. This new Statement will allow companies to carry most financial assets or financial liabilities at fair value, with changes recorded through earnings. This Statement represents the first phase of a multiyear project. The second phase, which is likely to be more controversial, will address the option to record certain nonfinancial assets and liabilities at fair value.

FASB Statement No. 156, *Accounting for Servicing of Financial Assets*

AFFECTS: Mortgage companies and other entities that service financial assets.

SUMMARY: Statement 156 requires that an entity separately recognize a servicing asset or a servicing liability when it undertakes an obligation to service a financial asset under a servicing contract in certain situations. Such servicing assets or servicing liabilities must be **initially measured at fair value**, if practicable. Statement 156 also allows an entity to choose one of two methods when subsequently measuring its servicing assets and servicing liabilities: (1) the *amortization method* or (2) the *fair value measurement method*. The amortization method existed under Statement 140 and remains unchanged in (1) allowing entities to amortize their servicing assets or servicing liabilities in proportion to and over the period of estimated net servicing income or net servicing loss and (2) requiring the assessment of those servicing assets or servicing liabilities for impairment or increased obligation on the basis of fair value at each reporting date. The fair value measurement method allows entities to measure their servicing assets or servicing liabilities at fair value on each reporting date and report changes in fair value in earnings in the period the change occurs. The Statement permits a one-time reclassification of available-for-sale securities to trading securities by

entities with recognized servicing rights upon initial adoption, provided that certain criteria are met.

DISCLOSURES: Servicing assets and servicing liabilities that are subsequently measured at fair value should be presented separately in the statement of financial position. Additional disclosures are required for all separately recognized servicing assets and liabilities.

EFFECTIVE: As of the beginning of an entity's first fiscal year that begins after September 15, 2006. Earlier adoption is permitted as of the beginning of an entity's fiscal year as long as the entity has not yet issued financial statements (including financial statements for any interim period) for that fiscal year.

TRANSITION: The requirements for recognition and initial measurement of servicing assets and servicing liabilities should be applied prospectively to all transactions after adoption. An entity that elects to subsequently remeasure its servicing assets and servicing liabilities at fair value should apply that election prospectively to all new and existing separately recognized servicing assets and servicing liabilities. The effects of remeasuring existing servicing assets and servicing liabilities should be reported as a cumulative-effect adjustment to retained earnings as of the beginning of the fiscal year and should be disclosed separately. Any gains or losses included in accumulated other comprehensive income associated with the reclassified available-for-sale securities should also be reported as a cumulative-effect adjustment to retained earnings as of the beginning of the fiscal year of adoption.

OTHER RESOURCES: Deloitte & Touche's [Heads Up](#) on Statement 156. Also, the FASB's [document](#) on revisions made to related authoritative literature because of the issuance of Statement 156.

FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*

AFFECTS: Companies that hold or issue financial instruments with embedded derivatives that otherwise would require bifurcation and companies that invest in securitized financial assets.

SUMMARY: Statement 155 relieves entities from separately determining the fair value of an embedded derivative that **would otherwise have to be bifurcated** from its host contract in accordance with Statement 133. Statement 155 allows an entity to make an **irrevocable election** to measure such a hybrid financial instrument at fair value in its entirety, with changes in fair value recognized in earnings. The election may be made on an instrument-by-instrument basis and can be made only when a hybrid financial instrument is initially recognized or when certain events occur that constitute a remeasurement (i.e., new basis) event for a previously recognized hybrid financial instrument. An entity must document its election to measure a hybrid financial instrument at fair value, either concurrently or via a preexisting policy for automatic election. Once the fair value election has been made, that hybrid financial instrument may not be designated as a hedging instrument pursuant to Statement 133.

In addition, Statement 155 requires that interests in securitized financial assets be evaluated to identify whether they are freestanding derivatives or hybrid financial instruments containing an embedded derivative that requires bifurcation (previously, these were exempt from Statement 133). With respect to determining whether an interest in securitized financial assets is a hybrid financial instrument, Statement 155 does not consider a concentration of credit risk, in the form of subordination of one interest in securitized assets to another, to be an embedded derivative.

DISCLOSURES: Hybrid financial instruments that are measured at fair value in their entirety should be presented separately in the statement of financial position. An entity must also provide information about the effect of changes in fair value on earnings. The gross gains and losses that make up the cumulative-effect adjustment upon adoption must be separately disclosed and determined on an instrument-by-instrument basis.

EFFECTIVE: For all financial instruments acquired, issued, or subject to a remeasurement (new basis) event occurring after the beginning of an entity's first fiscal year that begins after September 15, 2006. Upon adoption, an entity may elect fair value measurement for existing financial instruments with embedded derivatives that had previously been bifurcated pursuant to Statement 133. Early adoption is permitted as of the beginning of an entity's fiscal year as long as the entity has not yet issued financial statements (including financial statements for any interim period) for that fiscal year.

TRANSITION: Upon adoption, any difference between the total carrying amount of the individual components of the existing bifurcated hybrid financial instrument and the fair value of the combined hybrid financial instrument should be recognized as a cumulative-effect adjustment to beginning retained earnings. Prior periods should not be restated.

OTHER RESOURCES: Deloitte & Touche's [Heads Up](#) on Statement 155.

FSP on Accounting for Registration Payment Arrangements

AFFECTS: Issuers that engage in registration payment arrangements.

SUMMARY: The FASB has issued FSP EITF 00-19-2, which addresses an issuer's accounting for registration payment arrangements. The FSP clarifies that a registration payment arrangement and the financial instrument(s) subject to that arrangement should be separately measured and recognized. In addition to examples of separate measurement and recognition, the FSP provides transition guidance.

Paragraphs 7–11 of FSP EITF 00-19-2 discuss the recognition and measurement requirements. Paragraph 8 states, in part, that “an entity should recognize and measure a registration payment arrangement as a separate unit of account from the financial instrument(s) subject to that arrangement.” The FSP clarifies that such financial instrument(s) should be accounted for under other applicable GAAP, such as those in Opinion 21, Statement 133, and Issue 00-19, “without regard to the contingent obligation to transfer consideration pursuant to the registration payment arrangement.” It also states that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement should be separately recognized and measured in accordance with Statement 5 and Interpretation 14.

This FSP amends certain accounting literature to include scope exceptions for registration payment arrangements by adding the following:

- Paragraph 10(j) to Statement 133.
- Paragraph 17A to Statement 150.
- Paragraph 6(g) to Interpretation 45.

EFFECTIVE: This FSP's guidance is effective immediately for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified after December 21, 2006. Otherwise, the guidance is effective for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years.

TRANSITION: The effect of adopting the FSP should be recorded as a change in accounting principle through a cumulative-effect adjustment to retained earnings. Retrospective application of the guidance in this FSP to financial statements for earlier interim or annual periods is not permitted.

DISCLOSURES: In addition to disclosures required by other applicable GAAP, FSP EITF 00-19-2 requires the issuer of a registration payment arrangement to disclose the information required by paragraph 12 of the FSP, regardless of the likelihood of payment under the arrangement.

FASB Clears and Revises Statement 133 Implementation Issues

AFFECTS: Entities that apply cash flow hedging.

SUMMARY: The FASB recently cleared Implementation Issue G26, stating that an entity may designate the risk in a cash flow hedge as the risk of overall changes in the hedged cash flows related to the variable-rate financial asset or liability, but not as the interest-rate risk.

While clearing Implementation Issue G26, the Board identified a practice issue related to Implementation Issue G19 that necessitated deleting the sentence “Those short-term instruments are not ‘indexed’ to any market rate” from the “Commercial Paper” heading in the “Background” section of Implementation Issue G19. According to the FASB, this sentence was causing confusion.

EFFECTIVE: Implementation Issue G26 is effective on the first day of an entity's first fiscal quarter beginning after January 8, 2007.

Redeemable and Convertible Instruments

EITF Issue No. 05-1, “Accounting for the Conversion of an Instrument That Became Convertible Upon the Issuer’s Exercise of a Call Option”

AFFECTS: Companies that issue contingently convertible debt instruments and certain other instruments that are not currently convertible pursuant to their terms but become convertible upon the issuer’s exercise of a call option.

SUMMARY: Issue 05-1 addresses whether the conversion of such debt instruments into issuer shares should be accounted for as a conversion or an extinguishment. The Task Force concluded that the call option and the resulting equity securities issued should be accounted for as a conversion (i.e., no gain or loss recorded), provided that the debt instrument, **at issuance**, contains a substantive conversion feature (i.e., it is at least **reasonably possible** that it will become exercisable if the issuer is unable to call the instrument). Otherwise the transaction should be recorded as a debt extinguishment.

EFFECTIVE: For all conversions within the scope of the Issue that result from the exercise of call options in interim or annual reporting periods beginning after June 28, 2006.

TRANSITION: For instruments issued before June 28, 2006, the assessment of whether a substantive conversion feature exists at issuance should be based only on assumptions, considerations, and marketplace information available as of the issuance date. Early application is permitted for companies for which financial statements have not yet been issued. Retrospective application is not permitted.

OTHER RESOURCES: Deloitte & Touche’s [June 2006 EITF Roundup](#).

EITF Issue No. 06-6, “Debtor’s Accounting for a Modification (or Exchange) of Convertible Debt Instruments”

AFFECTS: Issuers that modify the terms of (or that exchange) convertible debt instruments that contain an embedded conversion option not accounted for as a derivative under Statement 133.

SUMMARY: Issue 96-19 provides guidance on determining whether the modification (or exchange) of a debt instrument results in a new debt instrument that is “substantially different” from the original and therefore treated as an extinguishment of the original debt, which typically results in a gain or loss. If the present value of the new instrument’s cash flows differs by at least 10 percent from that of the original (the “cash flow test”), the debt instruments are considered substantially different — and extinguishment accounting is required.

Issue 05-7 expanded the cash flow test to capture — as a cash flow — the fair value change of an embedded conversion option resulting from a modification (or exchange). In most modifications or exchanges, however, the lender and borrower exchange equal value. Accordingly, the change in the conversion option’s fair value is offset by the consideration paid or received to affect the change, and substantially different instruments are not identified as such.

In Issue 06-6, the EITF reached a consensus that when this offsetting effect is addressed, the change in fair value of a conversion option associated with a modification (or exchange) should not be included in the cash flow test. However, if the cash flow test does not result in an extinguishment, a second test is required. In the second test, the issuer compares the change in fair value of the embedded conversion option — calculated as the difference between the conversion option’s fair value immediately before and after the modification (or exchange) — to the carrying amount of the original debt instrument immediately before the modification (or exchange). If the change in fair value is at least 10 percent of the carrying amount of the original debt, the instruments are considered substantially different, resulting in extinguishment accounting.

Finally, any modification (or exchange) that adds or eliminates a “substantive” conversion option (with “substantive” contemplated in the context of Issue 05-1) also results in substantially different instruments.

If, after the three tests described above are applied, a modification (or exchange) does not result in an extinguishment, an increase in the conversion option’s fair value should be recognized as a reduction in the carrying amount of the debt, with a corresponding increase in additional paid-in capital. A decrease in the fair value of the conversion option should **not** be recognized.

EFFECTIVE: For modifications (or exchanges) occurring in interim or annual reporting periods beginning after November 29, 2006. Early application is permitted for modifications (or exchanges) occurring in periods for which financial statements have not been issued.

TRANSITION: Apply prospectively. Retrospective application to prior-year financial statements is not permitted.

EITF Issue No. 06-7, "Issuer's Accounting for a Previously Bifurcated Conversion Option in a Convertible Debt Instrument When the Conversion Option No Longer Meets the Bifurcation Criteria in FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities"

AFFECTS: Convertible debt issuers with previously bifurcated conversion options that no longer require separate derivative accounting under Statement 133.

SUMMARY: If a convertible debt instrument's embedded conversion option fails to satisfy the criteria in paragraph 12 of Statement 133, the conversion option requires bifurcation from the debt instrument (and recognition as a derivative liability). Frequently, share settlement restrictions, such as an insufficient amount of authorized and unissued shares to share-settle all existing commitments, result in bifurcation of a conversion option (see Issue 00-19). However, if the criteria that resulted in bifurcation are later satisfied (e.g., sufficient shares are now available to effect share settlement), derivative accounting no longer applies. At issue is how to account for the removal of the derivative liability.

In Issue 06-7, the Task Force affirmed its tentative conclusion, reaching a consensus that when a conversion option no longer requires separate accounting, the derivative liability should be reclassified to shareholders' equity. Any debt discount should continue to be amortized over the remaining term of the debt. As a result, the effective interest rate on the debt instrument will continue to exceed its coupon rate.

The Task Force reached a consensus that when a holder exercises a previously bifurcated conversion option, any remaining unamortized debt discount should be recognized immediately as interest expense. This approach is consistent with that of settling an instrument with the characteristics of "Instrument C" in Issue 03-7. Also, when a debt instrument with a previously bifurcated conversion option is extinguished for cash (or other assets) prior to its stated maturity, the reacquisition price should first be charged to shareholders' equity on the basis of the conversion option's fair value on the extinguishment date. Any residual should then be allocated to the debt extinguishment in determining the amount of gain or loss.

Finally, the Task Force reached a consensus that when a previously bifurcated conversion option no longer requires separate accounting, the issuer shall disclose (1) a description of the change causing the conversion option to no longer require bifurcation and (2) the amount of the derivative liability reclassified to shareholders' equity.

EFFECTIVE: Interim and annual periods beginning after December 15, 2006. Early application is permitted for periods in which financial statements have not been issued. Retrospective application is permitted.

TRANSITION: Apply prospectively to all previously bifurcated conversion options that no longer require bifurcation.

Consolidations

Although Interpretation 46(R) was issued late in 2003, it continued to affect standard-setting activity related to consolidations in 2006. The FASB issued an FSP on determining variability to be considered in applying the Interpretation. In addition, the EITF reached a consensus regarding the reporting of changes in differences between the fiscal year end of a parent company and a consolidated entity, while the AICPA released a few TPAs on the topic.

FASB Staff Position No. FIN 46(R)-6, "Determining the Variability to Be Considered in Applying FASB Interpretation No. 46(R)"

AFFECTS: Companies with interests in variable interest entities (VIEs).

SUMMARY: FSP FIN 46(R)-6 introduces the **by-design approach** to determine the variability to consider when applying Interpretation 46(R).

As a general rule, assets and operations of an entity create its variability while its liabilities and equity interests absorb that variability. Other contracts or arrangements entered into by the entity may appear to both create and absorb variability (for example, interest rate swaps) because they can be assets or liabilities depending on prevailing market conditions. In addition, a contract or arrangement may absorb many different types of risks (e.g., credit risk, interest rate risk, and foreign currency exchange risk). The by-design approach is used to determine which risk or risks are important in evaluating whether an interest is a variable interest under Interpretation 46(R). The analysis should focus on the role of a contract or arrangement in the design of the entity rather than on its legal form or accounting classification.

The FSP requires an analysis of the design of the entity in determining the variability to be considered in applying Interpretation 46(R), and provides the following two steps:

1. Analyze the nature of the risks in the entity.
2. Determine the purpose(s) for which the entity was created and determine the variability (created by the risks identified in step 1).

EFFECTIVE: For all entities (including newly created entities) with which an enterprise first becomes involved, and for all entities previously required to be analyzed under Interpretation 46(R) when a reconsideration event has occurred beginning the first day of the first reporting period beginning after June 15, 2006. Earlier application is permitted for periods for which no financial statements have yet been issued.

TRANSITION: Prospective application. Retrospective application is permitted, but not required. If retrospective application is elected, it must be completed no later than the end of the first annual reporting period ending after July 15, 2006.

OTHER RESOURCES: Deloitte & Touche's *Heads Up* on FSP FIN 46(R)-6.

EITF Issue No. 06-9, "Reporting a Change in (or the Elimination of) a Previously Existing Difference Between the Fiscal Year-End of a Parent Company and That of a Consolidated Entity or Between the Reporting Period of an Investor and That of an Equity Method Investee"

AFFECTS: Entities that change, or eliminate, differences in a reporting period between a parent company and a consolidated entity or between an investor and an equity method investee. Issue 06-9 does not apply to situations in which a parent company (or investor) changes its fiscal year end.

SUMMARY: In practice, there are differences in how changes are recognized in a consolidated subsidiary's or equity method investee's reporting period. Before Statement 154, these changes, regardless of their characterization, were typically recorded as a cumulative-effect adjustment to opening retained earnings in the year of change. However, if the change is considered a change in accounting principle, Statement 154 requires retrospective application to all prior-period financial statements presented.

The Task Force reached a consensus that a change in a subsidiary's or equity method investee's reporting period is a change in accounting principle. Therefore, the parent or investor should recognize the effects of the change through retrospective application to all prior periods presented pursuant to Statement 154.

EFFECTIVE: Changes occurring in interim or annual reporting periods beginning after November 29, 2006. Early application is permitted for periods in which financial statements have not been issued.

TRANSITION: Apply as a change in accounting principle through retrospective application of Statement 154.

AICPA TPA on Consolidated Financial Statements

AFFECTS: Companies that consolidate one or more subsidiaries.

SUMMARY: **TIS Section 1400.32, "Parent-Only Financial Statements and Relationship to GAAP"** — If consolidated financial statements are required under GAAP, under no circumstances may an entity prepare parent-company-only financial statements in place of consolidated financial statements and still be in compliance with GAAP.

AICPA TPAs on Consolidation of Variable Interest Entities

AFFECTS: Companies with interests in VIEs.

SUMMARY: **TIS Section 1400.29, "Consolidated Versus Combined Financial Statements Under FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities"** — A reporting entity that is the primary beneficiary of a VIE under Interpretation 46(R) should not issue combined financial statements (including the VIE); rather, the primary beneficiary should issue consolidated financial statements.

TIS Section 1400.30, "Stand-Alone Financial Statements of a Variable Interest Entity" — In certain circumstances, it may be appropriate to issue stand-alone financial statements of a VIE (i.e., subsidiary-only financial statements).

TIS Section 1400.31, "GAAP Departure for FIN No. 46(R)" — The failure of the primary beneficiary of a VIE under Interpretation 46(R) to consolidate that VIE should be considered a departure from GAAP. A qualified or adverse opinion should be issued to the extent that the effects of the departure are considered material to the financial statements.

TIS Section 1500.06, "Application of FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities, to Income Tax Basis Financial Statements" — The consolidation provisions of Interpretation 46(R) do not apply to financial statements prepared on an income tax basis. The Internal Revenue Code (IRC) provides guidance on income tax basis financial statements, and the threshold for consolidation under the IRC is 80 percent ownership. The required disclosures of Interpretation 46(R) should be made, or enough information should be provided to communicate the substance of those disclosures, in income tax basis financial statements.

Income Taxes

Enterprises typically take tax positions that may or may not be upheld if examined by the taxing jurisdiction. Statement 109 does not provide specific guidance on how such uncertainties should be reflected in an enterprise's financial statements. This lack of guidance has resulted in diversity in how enterprises recognize, derecognize, and measure potential tax benefits associated with tax positions. Therefore, to increase comparability in financial reporting of income taxes, the FASB issued Interpretation 48. This Interpretation, as well as other guidance issued throughout the year related to income taxes, is summarized below.

FASB Final Interpretation on Accounting for Uncertainty in Income Taxes

AFFECTS: All companies with tax positions accounted for in accordance with Statement 109.

SUMMARY: The FASB's objective in issuing Interpretation 48 is to increase comparability in financial reporting of income taxes. Although the validity of an enterprise's tax position is a matter of tax law, in certain cases the law is subject to significant and varied interpretation. As a result, an enterprise may be uncertain about whether a tax position would ultimately be sustained as filed in its tax return. Statement 109 does not provide specific guidance on how such uncertainties should be reflected in an enterprise's financial statements. This lack of guidance has resulted in diversity in how enterprises recognize, derecognize, and measure potential tax benefits associated with tax positions.

Interpretation 48 applies to all tax positions that are within the scope of Statement 109 and establishes a two-step approach for recognizing and measuring tax benefits. In step one, the Interpretation establishes a "more-likely-than-not" recognition threshold that must be met before a tax benefit can be recognized in the financial statements. To meet this threshold, the enterprise must determine that upon examination by the taxing authority, the tax position will more likely than not be sustained, based on the technical merits of the position. Once the recognition threshold has been met, enterprises will move to step two. In step two, enterprises are required to recognize the largest amount of tax benefit that is more than 50 percent likely to be realized upon ultimate settlement with the taxing authority. In both steps, enterprises must presume that the taxing authority has full knowledge of all relevant information.

Interpretation 48 also requires enterprises to make explicit disclosures at the end of each reporting period about uncertainties in their income tax positions, including a detailed rollforward of tax benefits taken that do not qualify for financial statement recognition.

EFFECTIVE: Interpretation 48 is effective for fiscal years beginning after December 15, 2006. Earlier adoption is permitted as of the beginning of an enterprise's fiscal year, provided that the enterprise has not yet issued financial statements, including interim period financial statements, for that fiscal year.

TRANSITION: Apply to all tax positions upon initial adoption. The cumulative effect of applying the provisions of the Interpretation should be reported as an adjustment to the opening balance of retained earnings for that fiscal year.

OTHER RESOURCES: Deloitte & Touche's [Heads Up](#) on Interpretation 48.

EITF Issue No. 06-3, "How Taxes Collected From Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross Versus Net Presentation)"

AFFECTS: Companies with taxes imposed concurrently on a specific revenue-producing transaction between a seller and a customer.

SUMMARY: The Task Force concluded that entities should present these taxes in the income statement on either a gross or a net basis in accordance with **their accounting policy**.

DISCLOSURES: Companies shall disclose their accounting policy pursuant to Opinion 22. In addition, if such taxes are significant and are presented on a gross basis, the amounts of those taxes should be disclosed.

EFFECTIVE: For financial statements for interim and annual periods beginning after December 15, 2006.

TRANSITION: Issue 06-3 only requires the presentation of additional disclosures. A company is not required to reevaluate its existing policies related to taxes within the Issue's scope. If a company chooses to reevaluate its existing policies and elects to change the presentation of taxes within the scope of this Issue, it must follow the requirements of Statement 154. Accordingly, a change would need to be deemed preferable.

OTHER RESOURCES: Deloitte & Touche's [June 2006 EITF Roundup](#).

New Texas Margin Tax (House Bill 3) Affects Tax Accounting as of May Enactment Date

AFFECTS: Taxable entities that do business in Texas or are chartered or organized in the state.

SUMMARY: On May 18, 2006, the State of Texas enacted House Bill 3 (the "Bill"), which replaces the state's current franchise tax with a "margin tax." The margin tax is assessed at 1 percent of Texas-sourced taxable margin (except for retailers and wholesalers, which will be assessed at 0.5 percent). The taxable margin is computed as the lesser of (1) 70 percent of total revenue or (2) total revenue less (a) cost of goods sold or (b) compensation. Definitions of and guidance on the terms "revenue," "cost of goods sold," and "compensation" are provided in the bill.

Although the Bill states that the new tax is not an income tax, it has characteristics of an income tax and should be accounted for as such under Statement 109. Paragraph 18 of Statement 109 indicates that a deferred tax asset or liability should be measured by using the enacted tax rate(s) expected to apply to taxable income in the periods in which the deferred tax asset or liability is expected to be realized or settled. Therefore, if an entity expects to be subject to more than one measure of taxable margin in the future, it may be required to schedule the reversal of those temporary differences to measure the related deferred tax asset or liability. The Bill also provides for a temporary margin tax credit that can be claimed against margin tax due. This credit should be recognized as a deferred tax asset (subject to realizability under Statement 109).

EFFECTIVE: For returns originally due on or after January 1, 2008. However, as required by Statement 109, all effects of a tax law change should be accounted for in the period of the law's enactment (i.e., the reporting period that includes May 18, 2006).

OTHER RESOURCES: [Worksheet](#) to calculate the Texas margin tax and Deloitte Tax LLP's [Alert](#) on the Texas margin tax.

Practice Guide: FASB Interpretation 48

AFFECTS: Financial statement preparers, auditors, and tax advisers.

SUMMARY: The AICPA issued *Practice Guide on Accounting for Uncertain Tax Positions Under FIN 48*. Although not authoritative, the guide gives the reader a general overview of the requirements of Interpretation 48.

AICPA TPA on Income Taxes

AFFECTS: Entities that make contributions to certain nonprofit scholarship funding organizations and their auditors.

SUMMARY: TIS Section 5700.01 relates to income tax accounting for contributions to certain nonprofit scholarship funding organizations. The TPA states that an entity should report such amounts as contributions in its income statement in accordance with Statement 116.

Insurance

FASB Staff Position No. FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors"

AFFECTS: Investors in life settlement contracts.

SUMMARY: In a life settlement contract, a life settlement provider or a broker (collectively, the "investor") pays an amount in excess of the cash surrender value of a life insurance policy to the insured party. The investor may also continue to make premium payments on the policy. In exchange, the investor receives payment on the policy when the insured dies.

Investors have historically accounted for these transactions under Technical Bulletin 85-4. That is, they expensed, upon purchase, the difference between the purchase price paid to the insured and the cash surrender value of the life settlement contract. In addition, they reported the amount that could have been realized under the insurance contract as an asset.

FSP FTB 85-4-1 allows an investor to account for its investment in a life settlement contract by using either the investment method or the fair value method in periods subsequent to the initial recognition of the investment. The election is irrevocable and should be made on an instrument-by-instrument basis. Investments accounted for under the investment method are initially recorded at transaction price (the amount the investor pays to the insured party) plus any initial direct external costs. Subsequent costs to keep the policy in force are capitalized to the carrying amount. When the insured dies, the investor recognizes, in the income statement, the difference between the carrying amount of the investment in the life settlement contract and the life insurance proceeds of the underlying life insurance policy. Investments accounted for under the fair value method are initially recorded at transaction price and are subsequently remeasured to fair value each reporting period, with changes in fair value recognized in earnings in the period of the change.

DISCLOSURES: Investors shall report amounts for investments that are measured at fair value separately from amounts that are accounted for under the investment method on the face of the financial statements.

Investors in life settlement contracts should disclose the following:

- The number of life settlement contracts.
- The carrying value of the settlement contracts.
- The face value (death benefits) of the life insurance policies underlying the contracts.

The FSP includes additional disclosure requirements that are specific to investments accounted for under either the investment method or the fair value method.

EFFECTIVE: Effective for fiscal years beginning after June 15, 2006. Earlier application is permitted as of the beginning of an entity's fiscal year as long as no financial statements have been issued (including interim financial statements) for that fiscal year.

TRANSITION: Prospective application is required for all new investments in life settlement contracts, and a cumulative-effect adjustment to retained earnings should be made at the date of adoption to recognize the impact on existing life settlement contract investments.

EITF Issue No. 06-5, “Accounting for Purchases of Life Insurance — Determining the Amount That Could Be Realized in Accordance With FASB Technical Bulletin No. 85-4, *Accounting for Purchases of Life Insurance*”

AFFECTS: Entities with life insurance policies, including corporate-owned or business-owned life insurance.

SUMMARY: In Issue 06-5, a determination of the amount that could be realized under an insurance contract should (1) consider any additional amounts (beyond cash surrender value) included in the contractual terms of the policy and (2) be based on assumed surrender at the individual policy or certificate level, unless all policies or certificates are required to be surrendered as a group. When it is probable (as defined in Statement 5) that contractual restrictions would limit the amount that could be realized, such contractual limitations should be considered. Any amounts recoverable at the insurance company’s discretion should be excluded from the amount that could be realized.

Fixed amounts recoverable in excess of one year should be recorded at their present values in accordance with Opinion 21. Fixed amounts exclude the cash surrender value component of the policy, including situations in which a contractual restriction may limit the entity’s ability to surrender the policy. Said another way, provided the cash surrender value component continues to be credited with interest during the time of the restriction — that is, it does not become “fixed” — it should not be discounted in accordance with Opinion 21. However, any such contractual restrictions on surrender should be disclosed.

EFFECTIVE: Fiscal years beginning after December 15, 2006. Earlier application is permitted as of the beginning of a fiscal year for periods in which interim or annual financial statements have not been issued.

TRANSITION: Entities should recognize the effects of applying the consensus through either (1) a change in accounting principle through a cumulative-effect adjustment to retained earnings or to other components of equity or net assets as of the beginning of the year of adoption, or (2) a change in accounting principle through retrospective application to all prior periods.

Investment Companies

AICPA Statement of Position 06-1, *Reporting Pursuant to the Global Investment Performance Standards*

AFFECTS: Practitioners that perform attestation engagements for investment management firms.

SUMMARY: SOP 06-1 supersedes SOP 01-4 and provides guidance on attestation engagements on an investment management firm’s compliance with voluntary industry standards for calculating and reporting performance.² The guidance applies both to “verification engagements,” which relate to attestation engagements on firm-wide compliance with performance standards, and to “performance examinations,” which relate to the performance of an aggregation of a number of portfolios into a single group that represents a particular investment objective or strategy (referred to in the SOP as a “composite” or “composite construction”). Examples of engagement letters, management representation letters, and attest reports are also included in the SOP.

EFFECTIVE: April 6, 2006.

² Note that as of January 1, 2006, the Association for Investment Management and Research Performance Presentation Standards converged with the Certified Financial Analysts Institute’s Global Investment Performance Standards (GIPS).

AICPA TPAs on Nonregistered Investment Partnerships

AFFECTS: Nonregistered investment partnerships.

SUMMARY: **TIS Section 6910.16, “Presentation of Boxed Investment Positions in the Condensed Schedule of Investments of Nonregistered Investment Partnerships”** — Long and short positions in the same security (“boxed positions”) should be evaluated on a gross basis for the purposes of performing the 5-percent-of-net-assets test³ in determining the appropriate level of disclosure and presentation in the schedule of investments.

TIS Section 6910.17, “Disclosure of Long and Short Positions — Nonregistered Investment Partnerships” — Total long and total short positions in any one issuer should be considered separately for disclosure in the condensed schedule of investments. That is, if a nonregistered investment partnership has a long position that exceeds 5 percent of net assets and a short position in the same issuer that is less than 5 percent of net assets, disclosure of the long position is required while disclosure of the short position is not.

TIS Section 6910.18, “Disclosure of an Investment in an Issuer When One or More Securities and/or One or More Derivative Contracts Are Held — Nonregistered Investment Partnerships” — If a nonregistered investment partnership holds (a) one or more securities of the same issuer and (b) one or more derivative contracts for which the underlying is a security of the same issuer, such securities and derivative contracts should be presented in the condensed schedule of investments on a basis consistent with the classification of the securities or contracts on the statement of assets and liabilities. Securities and derivative contracts that are classified as assets should be aggregated. If the sum exceeds 5 percent of net assets, each position should be separately disclosed on the condensed schedule of investments. Liability positions should be treated similarly. The TPA provides several examples.

TIS Section 6910.19, “Information Required to Be Disclosed in Financial Statements When Comparative Financial Statements of Nonregistered Investment Partnerships Are Presented” — The AICPA Audit and Accounting Guide, *Audits of Investment Companies*, does not require comparative financial statements for nonregistered investment partnerships. However, if an entity elects to prepare comparative financial statements, the schedule of investments for the prior year should also be included.

TIS Section 6910.20, “Presentation of Purchases and Sales/Maturities of Investments in the Statement of Cash Flows — Nonregistered Investment Partnerships” — In general, a nonregistered investment partnership should present purchases and sales/maturities of long-term investments (securities purchased with no stated maturity or with a stated maturity of greater than one year at the date of acquisition) on a gross basis in the statement of cash flows. Purchases and sales/maturities of short-term investments, however, may be presented on a net basis.

AICPA TPAs on Investment Companies

AFFECTS: Investment companies and their auditors.

SUMMARY: **TIS Section 6910.21, “Recognition of Premium/Discount on Short Positions in Fixed-Income Securities”** — This TPA discusses the recognition of premium/discount on short positions in fixed-income securities. The TPA states that when recognizing interest income on short positions, investment companies should recognize all economic elements of interest, including premium and discount.

TIS Section 6910.22, “Presentation of Reverse Repurchase Agreements” — This TPA discusses the presentation of reverse repurchase agreements. The TPA states that a reverse repurchase agreement should be presented at amounts payable. Moreover, it indicates that if such an agreement is denominated in a currency different from the reporting currency, the current exchange rate should be used during translation.

TIS Section 6910.23, “Accounting Treatment of Offering Costs Incurred by Investment Partnerships” — This TPA discusses accounting treatment of offering costs incurred by investment partnerships. The TPA states that an investment partnership that continually offers its interests should defer

³ The 5-percent-of-net-assets test is described in paragraph 7.13 of the AICPA Audit and Accounting Guide, *Audits of Investment Companies*.

offering costs incurred before operations began and amortize these costs to expense over the period — up to a maximum of 12 months — in which it continually offers its interests.

TIS Section 6910.24, “Meaning of ‘Continually Offer Interests’” — This TPA defines “continually offer interests,” stating that an investment partnership is thought to continually offer its interest if an eligible, new investor (i.e., one that does not already own interest in the partnership) may enter into an agreement to purchase an interest in the partnership on any one business day or on a series of business days over a continuous period.

SEC Final Rule, *Fund of Funds Investments*

AFFECTS: Investment companies.

SUMMARY: The SEC has adopted three new rules within Final Rule Release 33-8713 under the Investment Company Act of 1940 (the “Investment Company Act”) that address the ability of an investment company (“fund”) to purchase shares of another fund. Currently, the Investment Company Act limits the ability of funds to invest in other funds, subject to certain exceptions. The Final Rules:⁴

- Allow funds to enter into “cash sweep arrangements” under which a fund may invest its available cash in a money market fund.
- Offer greater flexibility to a fund that invests primarily in funds of the same fund group.
- Offer greater flexibility for a fund that invests small amounts in many unaffiliated funds to structure the sales load it charges (but does not increase the overall amount charged).

In addition, the SEC has adopted amendments to investment company forms⁵ that require a “fund of funds” to disclose in its fee table the expenses charged by the purchased funds in aggregate.

EFFECTIVE: The Final Rules are effective July 31, 2006. All new registration statements filed on the investment company forms and all post-effective amendments that are annual updates to effective registration statements on the investment company forms filed on or after January 2, 2007, must include the disclosure required by the form amendments.

Cash Flows

AICPA Center for Public Company Audit Firms Alert #90, *SEC Staff Position Regarding Changes to the Statement of Cash Flows Relating to Discontinued Operations*

AFFECTS: Public companies reporting discontinued operations in their financial statements.

SUMMARY: At the 2005 AICPA National Conference on Current SEC and PCAOB Developments, an SEC staff member gave examples of acceptable and unacceptable presentations of cash flows related to discontinued operations. He indicated that it is not appropriate to present cash flows from discontinued operations as a single line item at the bottom of the statement of cash flows or entirely within operating activities (i.e., aggregating operating, investing, and financing cash flows).

⁴ The Final Rules include Rules 12d1-1, 12d1-2, and 12d1-3.

⁵ Amendments are made to Forms N-1A, N-2, N-3, N-4, and N-6.

Cash flows pertaining to discontinued operations should be separately disclosed either (1) **within each category** of the statement of cash flows or (2) near the bottom of the statement of cash flows, **by category**. Alternatively, companies choosing not to separately disclose cash flows pertaining to discontinued operations should present all cash flows (i.e., continuing and discontinued) within each category without differentiation.

Alert #90 states that changes to the statement of cash flows regarding the presentation of cash flows of a discontinued operation from an unacceptable presentation method to an acceptable presentation method should be treated as the correction of an error. However the SEC will not object to issuers retrospectively modifying their presentations in a manner similar to a change in accounting method with no reference to the correction of an error if the correction is made in the issuer's **first periodic report filed subsequent to February 15, 2006**. If the issue is discovered and corrected in a later interim or annual period, the change in presentation should be treated as a correction of an error with prior filings amended.

DISCLOSURES: If the change in presentation is treated as a change in accounting method, the financial statements may be marked "revised" or "restated," but the term "reclassified" should not be used. Specific footnote disclosure of the change must also be provided, and it is not acceptable to assert that the change is already encompassed by a general policy note statement.

AICPA Center for Public Company Audit Firms Alert #98, Update to SEC Staff Position Regarding Changes to the Statement of Cash Flows Relating to Discontinued Operations (Addendum to CPCA Alert #90)

AFFECTS: Public companies reporting discontinued operations in their financial statements.

SUMMARY: Alert #98 provides guidance on interim periodic reports and registration and proxy statements filed after February 15, 2006, with respect to situations discussed in Alert #90.

Alert #90, issued in February, discussed changing cash flow statements for inappropriate presentations of discontinued operations. Under that Alert, registrants were allowed to retrospectively modify their presentations in a manner similar to a change in accounting method. Alert #90 stipulated that corrections must be made in the next periodic report filed after February 15, 2006. Alert #98 discusses the **revisions and disclosures** required in interim periodic reports on Form 10-Qs filed after February 15, 2006. The Alert states that companies should (1) take Alert #90's presentation guidance into account when presenting the year-to-date information on Form 10-Qs and (2) revise the comparative prior-period condensed statement of cash flows to reflect the guidance noted in Alert #90 and label the information as **"revised" or "restated"** (if the company has not previously filed revised prior-period cash flow information).

DISCLOSURES: Generally, the Alert requires the following disclosures for Form 10-Qs and registration and proxy statements filed after February 15, 2006, but before an annual report on Form 10-K that includes revised cash flow presentation:

- The registrant's intent to revise its previously issued annual statements of cash flows in its next annual report.
- The reasons for the revisions.
- The quantitative effect of the revision on the three latest fiscal years (and the most recent interim-to-date period, if applicable).

Internal Control

AICPA SASs 104–111 on Risk Assessment Standards

AFFECTS: Auditors of nonpublic companies.

SUMMARY: The ASB issued eight SASs that enhance the connection between the risk of misstatement and the audit procedures performed:

- SAS No. 104, *Amendment to Statement on Auditing Standards No. 1, Codification of Auditing Standards and Procedures ("Due Professional Care in the Performance of Work")*.
- SAS No. 105, *Amendment to Statement on Auditing Standards No. 95, Generally Accepted Auditing Standards*.
- SAS No. 106, *Audit Evidence*.
- SAS No. 107, *Audit Risk and Materiality in Conducting an Audit*.
- SAS No. 108, *Planning and Supervision*.
- SAS No. 109, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*.
- SAS No. 110, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*.
- SAS No. 111, *Amendment to Statement on Auditing Standards No. 39, Audit Sampling*.

The primary objective of the SASs is to enhance auditors' application of the audit risk model. These SASs require auditors to obtain:

- A more in-depth understanding of an entity's environment, including its internal control environment, to identify (1) risks that may lead to a material misstatement in the financial statements and (2) how such risks are being mitigated by the entity.
- A more comprehensive assessment of the risks based on that understanding.
- An improved linkage between the identified risks and the nature, timing, and extent of audit procedures performed to address those risks.

EFFECTIVE: For audits of financial statements for periods beginning on or after December 15, 2006. Early adoption is permitted.

AICPA Statement on Auditing Standards No. 112 (AU Section 325), *Communicating Internal Control Related Matters Identified in an Audit*

AFFECTS: Auditors of nonpublic companies.

SUMMARY: SAS 112 provides **guidance to auditors of nonpublic companies** on communicating matters related to an entity's internal control over financial reporting identified in an audit, and supersedes SAS 60. Among other provisions, the SAS achieves consistency with PCAOB Auditing Standard 2 by:

- Incorporating the defined terms "control deficiency," "significant deficiency," and "material weakness."
- Including guidance on evaluating the severity of internal control deficiencies.
- Requiring the auditor to inform, in writing, management (and those charged with governance) of significant deficiencies and material weaknesses identified during an audit.

EFFECTIVE: For audits of financial statements for periods ending on or after December 15, 2006.

Conforming Changes Made to Standard on Reporting on a Nonissuer's Internal Control Over Financial Reporting to Achieve Consistency With SAS 112

AFFECTS: Nonissuers and their auditors.

SUMMARY: The AICPA has made conforming changes to AT Section 501 that incorporate relevant terms, definitions, and guidance to achieve consistency with the recently issued SAS 112. These changes are as follows:

- Deleting the term "reportable condition" and its definition.
- Replacing the definition of the term "material weakness."
- Introducing the terms "control deficiency" and "significant deficiency" and their related definitions.
- Replacing the guidance on evaluating control deficiencies with the relevant guidance from SAS 112.
- Replacing the term "audit committee" with the term "those charged with governance" (defined in SAS 103) to describe the party to whom the practitioner must communicate significant deficiencies and material weaknesses.
- Identifying areas in which a control deficiency constitutes a significant deficiency in internal control.
- Identifying indicators of a control deficiency that should be regarded as at least a significant deficiency and a strong indicator of a material weakness in internal control.
- Requiring the practitioner to communicate to management and those charged with governance, in writing, significant deficiencies and material weaknesses.

EFFECTIVE: The conforming changes are effective when the subject matter or assertion is as of, or for the period ending on or after, December 15, 2006, with earlier application permitted.

AICPA Audit Risk Alert on Understanding SAS 112

AFFECTS: Auditors of nonissuers.

SUMMARY: The AICPA issued an Audit Risk Alert to help auditors implement SAS 112. The Alert clarifies common misunderstandings regarding the application of SAS 112. The following concepts will assist with implementation:

- Auditors cannot be part of a client's internal control.
- Auditors cannot be a compensating control for the client.
- SAS 112 requires auditors to evaluate control deficiencies if they are identified, not to search for them.

AICPA Audit Guide on Assessing and Responding to Audit Risk

AFFECTS: Auditors of nonissuers.

SUMMARY: To help auditors of nonissuers assess risk in a financial statement audit performed in accordance with the ASB's generally accepted auditing standards, the AICPA issued an Audit and Accounting Guide, *Assessing and Responding to Audit Risk in a Financial Statement Audit*. The guide includes examples, flowcharts, observations, and suggestions. Although not authoritative, the guide may help the auditor understand and apply the SASs.

EFFECTIVE: For audits of financial statements for periods beginning on or after December 15, 2006. This guide supersedes the AICPA Audit Guide, *Consideration of Internal Control in a Financial Statement Audit* (new edition as of April 1, 1996).

PCAOB Auditing Standard No. 4, *Reporting on Whether a Previously Reported Material Weakness Continues to Exist*

AFFECTS: Public companies and their auditors.

SUMMARY: The SEC approved PCAOB Auditing Standard 4, which should be applied when an auditor is engaged to report on management's assertion that a previously reported **material weakness no longer exists** as of a specified date. These stand-alone engagements are **voluntary** and are performed as elected by a company's management. Before the approval of the Standard, the SEC solicited comments and received questions regarding the **acceptable forms** for filing management's report and the auditor's report. The SEC provided the following responses to the questions raised:

- SEC rules do not address the filing of such voluntary information; however, the use of any Securities Exchange Act of 1934 (the "Exchange Act") form the filer believes is appropriate may be used.
- The SEC's general disclosure principle and requirements would apply when the circumstances surrounding the remediation of a previously reported material weakness are described; however, the disclosure should not amend management's conclusion about the effectiveness of internal control over financial reporting as of the end of the fiscal year.
- If remediation was completed between the end of the fiscal year and the filing of the Form 10-K, management may include a single combined report on the results of the annual assessment of internal control over financial reporting and the subsequent conclusion regarding the remediation of a material weakness identified in the annual assessment.

EFFECTIVE: February 6, 2006.

COSO Issues Guidance on Internal Control Over Financial Reporting for Smaller Public Companies

AFFECTS: Smaller public companies and their auditors.

SUMMARY: The Committee of Sponsoring Organizations of the Treadway Commission (COSO) has issued *Internal Control Over Financial Reporting — Guidance for Smaller Public Companies*. The guidance does not replace or modify COSO's 1992 *Internal Control — Integrated Framework*, which has served as the internal control framework for many organizations' implementation of Section 404 of the Sarbanes-Oxley Act of 2002 (the "Act") and PCAOB Auditing Standard 2, but provides guidance on how smaller public companies should apply the framework. The guidance is divided into the following three volumes:

- An executive summary
- An overview of internal control over financial reporting in smaller businesses, including descriptions of company characteristics and how they affect internal control, challenges smaller businesses face, and how management can use the framework.
- Illustrative tools to assist management in evaluating internal control.

OTHER RESOURCES: [Executive Summary](#) and a [document](#) of the guidance.

Extension of Sarbanes-Oxley Act's Section 404 Compliance for Certain Companies

AFFECTS: Non-accelerated filers and newly public companies.

SUMMARY: The SEC issued a Final Rule extending deadlines for compliance with the Section 404 requirements of the Act and for the auditor's attestation for **non-accelerated filers**. The Final Rule extends the date by which non-accelerated filers must provide management's report assessing the effectiveness of the company's internal control over financial reporting from fiscal years ending on or after July 15, 2007, to fiscal years ending on or after December 15, 2007. The Final Rule also extends the effective date for the auditor's attestation report on internal control over financial reporting to the first annual report for a fiscal year ending on or after December 15, 2008.

In addition, the Final Rule provides a transition period for Section 404 compliance for all newly public companies (i.e., any company that has become public through an initial public offering or a registered

exchange offer or that otherwise has become subject to the reporting requirements of the Exchange Act, including a foreign private issuer that is listed on a U.S. exchange for the first time). Under the Final Rule, a newly public company, regardless of its size, will not be required to provide a management assessment or an auditor attestation report of internal control over financial reporting until it files its second annual report with the SEC.

EFFECTIVE: See summary section above for effective dates.

Extension of Sarbanes-Oxley Act's Section 404 Compliance for Certain Foreign Private Issuers

AFFECTS: Foreign private issuers with a public float between \$75 million and \$700 million as of the last day of their most recently completed second fiscal quarter.

SUMMARY: The Final Rule extends compliance for the auditor's attestation (Section 404(b) of the Act) for foreign private issuers (FPIs) that are accelerated filers (but not large accelerated filers) and that file their annual reports on a Form 20-F or Form 40-F.

EFFECTIVE: The compliance date for providing an auditor's attestation report on internal control over financial reporting in such an issuer's annual report is extended for an additional year, to fiscal years ending on or after July 15, 2007. However, management's report is still required for fiscal years ending on or after July 15, 2006. The Rule does not change the current requirements for compliance with Section 404 for large accelerated FPIs, which is for fiscal years ending on or after July 15, 2006.

OTHER RESOURCES: Deloitte & Touche's [Heads Up](#) on the Final Rule.

Loans

AICPA TPAs Regarding Loan Pool Accounting Under SOP 03-3

AFFECTS: Companies that apply SOP 03-3.

SUMMARY: **TIS Section 2130.36, "Impact on Cash Flows on a Group of Loans Accounted for as a Pool in Accordance With SOP 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer, If There Is a Confirming Event, and One Loan Is Removed as Expected"** — Gives an example of the impact on the accounting for a pool of loans if there is a confirming event (e.g., bankruptcy and default by an obligor) and one loan is removed as expected, but the investor does not change its original expectation of cash flows. The example indicates that the investor should remove the contractual cash flows from that loan and an equal amount of non-accretable difference from the pool such that the yield is unaffected. The TPA does not address charge-offs.

TIS Section 2130.37, "Impact on Cash Flows on a Group of Loans Accounted for as a Pool in Accordance With SOP 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer, If There Is a Confirming Event, One Loan Is Removed From the Pool, and the Investor Decreases Its Estimate of Expected Cash Flows" — Gives an example of the impact on the accounting for a group of loans accounted for as a pool if (1) there is a confirming event, (2) one loan is removed from the pool, and (3) the investor decreases its estimate of expected cash flows. The example indicates that the investor should record a provision in its loan loss allowance account for the present value of the expected cash flows of the loan being removed from the pool.

In addition, the investor should remove the contractual cash flows from that loan and an equal amount of non-accretable discount from the pool such that the yield is unaffected. The TPA does not address charge-offs.

Interagency Guidance Issued on Nontraditional Mortgage Products

AFFECTS: Financial institutions with “nontraditional” mortgage loans in their portfolios.

SUMMARY: Five federal financial regulatory agencies⁶ (the “Agencies”) issued final guidance on nontraditional mortgage product risks. Some of the risks posed by such nontraditional (also referred to as “alternative” or “exotic”) mortgage loans include permitting borrowers to defer repayment of principal and sometimes interest. These types of loans are typically known as “interest-only” mortgages and “payment option” adjustable-rate mortgages. Because of the lack of principal amortization and the potential for negative amortization, compounded with offering the products to the broader spectrum, the Agencies are concerned that borrowers may not fully understand the terms and risks. Therefore, they have issued this final guidance, which discusses the importance of managing the increased risks associated with these loans. The guidance suggests that management should:

- Ensure that terms and underwriting standards are in line with careful lending practices, including consideration of a borrower’s ability to repay.
- Perform under strong risk management standards and provide for allowances and capital levels that reflect the collectibility of the portfolios.
- Ensure that consumers have the right information to clearly understand the terms and risks associated with the products before making decisions.

OTHER RESOURCES: The Agencies also issued two additional related documents. One of the documents is [Proposed Illustrations of Consumer Information for Nontraditional Mortgage Products](#). The other document is an addendum to the [May 2005 Interagency Credit Risk Management Guidance for Home Equity Lending](#).

Revised Guidance Issued on the Allowance for Loan and Lease Losses

AFFECTS: All depository institutions supervised by the banking agencies, except U.S. branches and agencies of foreign banks, and institutions insured and supervised by the National Credit Union Administration.

SUMMARY: The Agencies responsible for supervising depository institutions recently issued a revised policy statement on the allowance for loan and lease losses (ALLL). The agencies are also issuing a document that includes frequently asked questions (FAQ) to help institutions apply GAAP and ALLL supervisory guidance, including the development and assessment of the ALLL estimate.

OTHER RESOURCES: The [revised ALLL policy statement](#) and the [ALLL FAQ document](#) are available on any of the agencies’ Web sites.

Property, Plant, and Equipment

FSP on Planned Major Maintenance Activities

AFFECTS: All companies with planned major maintenance activities.

SUMMARY: FSP AUG AIR-1 prohibits use of the accrue-in-advance method of accounting for planned major maintenance activities in annual and interim reporting periods (i.e., periodic major overhauls and maintenance of plant and equipment). It continues to permit the application of the other three alternative methods of accounting for planned major maintenance activities that are in the AICPA Audit and Accounting Guide, *Airlines* (“Airlines Guide”), and used by other industries: direct expense, built-in overhaul, and deferral. Although the FSP amends the Airlines Guide, the guidance in the FSP is applicable to entities in all industries.

⁶ The agencies included are Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision, and National Credit Union Administration.

According to the FASB, the accrue-in-advance method of accounting causes the recognition of a liability in a period prior to the occurrence of the transaction or event obligating the entity. Consequently, this recognition fails to conform to the definition of a liability found in Concepts Statement 6. However, the Board noted that a liability required to be recorded for an asset retirement obligation based on a legal obligation, as explained and illustrated in Statement 143 and Interpretation 47, does embody a liability. Therefore, the Board believes that if the event obligating the entity has occurred, the liability should be recorded.

In addition to amending the Airlines Guide, the FSP amends Opinion 28 to remove its reference in paragraph 16(a) to annual major repairs. The FSP requires disclosure of the method of accounting selected for planned major maintenance activities, as well as information regarding the change from the accrue-in-advance method to another method.

EFFECTIVE: The FSP is effective for the first fiscal year beginning after December 15, 2006. Earlier adoption is permitted as of the beginning of an entity's fiscal year.

TRANSITION: The FSP should be applied retrospectively for all financial statements presented, unless doing so is impracticable.

AICPA TPA on Liquidated Damages

AFFECTS: All entities and their auditors.

SUMMARY: **TIS Section 2210.28, "Accounting for Certain Liquidated Damages"** — Relates to accounting for liquidated damages by the buyer of property, plant, and equipment (PP&E). It states that the buyer should record liquidated damages as a reduction in the cost of PP&E.

Moreover, the TPA indicates that the buyer should recognize liquidated damages that exceed the cost of PP&E as income.

Other Accounting

FASB Staff Position No. FAS 126-1, "Applicability of Certain Disclosure and Interim Reporting Requirements for Obligors for Conduit Debt Securities"

AFFECTS: Entities that apply, or should apply, Statement 126.

SUMMARY: FSP FAS 126-1 amends certain accounting standards to clarify the definition of a "public entity." The definition now includes entities that are obligors for conduit debt securities, including those that participate in a pooled conduit debt security, and that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets). Any references in authoritative accounting literature to the definition of a public entity or enterprise that are not included in the list below are unaffected by this FSP. The specific accounting standards amended by this FSP are:

- APB Opinion No. 28, *Interim Financial Reporting*.
- FASB Statement No. 69, *Disclosures About Oil and Gas Producing Activities*.
- FASB Statement No. 109, *Accounting for Income Taxes*.
- FASB Statement No. 126, *Exemption From Certain Required Disclosures About Financial Instruments for Certain Nonpublic Entities*.
- FASB Statement No. 131, *Disclosures About Segments of an Enterprise and Related Information*.
- FASB Statement No. 132 (revised 2003), *Employers' Disclosures About Pensions and Other Postretirement Benefits*.

- FASB Statement No. 141, *Business Combinations*.
- AICPA Audit and Accounting Guide, *Health Care Organizations*.
- AICPA Audit and Accounting Guide, *Not-for-Profit Organizations*.

EFFECTIVE: For fiscal periods beginning after December 15, 2006. If an entity issues interim financial statements, the FSP shall be applied in the first interim period after the date of adoption.

TRANSITION: The FSP should be applied prospectively. If an entity elects to apply the guidance retrospectively, it must do so to all prior periods.

FSP on Accounting for a Change in Income Tax Cash Flows Generated by a Leveraged Lease Transaction

AFFECTS: All companies with leveraged leases.

SUMMARY: FSP FAS 13-2 gives guidance on a change or projected change in the timing of income tax cash flows relating to a leveraged lease as a result of a settlement with the IRS. Such a change shall result in a recalculation, at inception, of the lease rate of return and the allocation of income to positive investment years.⁷ The accounts constituting the net investment balance shall be adjusted to conform to the recalculated balances, and the change in the net investment shall be recognized as a gain or loss.

The FSP applies only to changes or projected changes in the timing of income taxes that are directly related to the leveraged lease transaction.

EFFECTIVE: Effective for fiscal years beginning after December 15, 2006. Earlier application is permitted as of the beginning of an entity's fiscal year, provided that the entity has not yet issued financial statements, including any interim financial statements, for that fiscal year.

TRANSITION: All recognized tax positions in a leveraged lease must be measured in accordance with Interpretation 48 at the date of adoption of this FSP. If, at the date of adoption, the application of Interpretation 48 causes a change in the recognition or measurement of the tax position, that change shall be considered a change of an assumption as of the date of adoption of the FSP. The cumulative effect of applying the provisions of this FSP shall be reported as an adjustment to the beginning balance of retained earnings as of the beginning of the period in which this FSP is adopted.

EITF Issue No. 06-1, "Accounting for the Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service From the Service Provider"

AFFECTS: Specialized service providers, such as certain cell phone or satellite media companies, that give consideration to manufacturers or resellers of equipment needed to obtain the service. For transactions within the scope of Issue 06-1, the service provider does not purchase or take title of the equipment, or sell the equipment directly to the end-customer.

SUMMARY: Consideration provided to a manufacturer or reseller should be characterized in the service provider's income statement on the basis of the form of consideration rendered to the end-customer as directed by the service provider. Consideration is deemed "directed by" the service provider if the manufacturer or reseller is contractually required to pass a specific form of consideration on to the end-customer (i.e., there is contractual linkage).

"Directed" consideration is characterized in the income statement based on Issue 01-9. That is, "cash consideration" is characterized as a reduction of revenue; "other than cash" consideration is characterized as an expense. If the form of consideration is not directed by the service provider, it should be characterized

⁷ Consistent with the guidance in paragraph 46 of FASB Statement No. 13, *Accounting for Leases*.

as “other than cash” (i.e., an expense). For purposes of applying this Issue, the term “cash consideration” does not include sales incentives (which would be considered “cash consideration” in Issue 01-9).

EFFECTIVE: First annual reporting period beginning after June 15, 2007. Early application is permitted for financial statements not yet issued.

TRANSITION: Apply the consensus as a change in accounting principle through retrospective application to all prior periods presented.

EITF Issue No. 06-8, “Applicability of the Assessment of a Buyer’s Continuing Investment Under FASB Statement No. 66, Accounting for Sales of Real Estate, for Sales of Condominiums”

AFFECTS: Condominium developers.

SUMMARY: Condominium developers often sell individual condominium units before completing the entire project; in such cases, the buyer makes a down payment at the time of contract signing. In accounting for such sales, developers apply either the percentage-of-completion method — provided that the criteria listed in paragraph 37 of Statement 66 are met — or the deposit method. One criterion in paragraph 37 requires that the sale price be deemed **collectible** and refers to paragraph 4 of Statement 66 in assessing collectibility. Paragraph 4, in turn, assesses collectibility through, among other considerations, demonstrating the buyer’s “substantial initial and continuing investments that give the buyer a stake in the property sufficient that the risk of loss through default motivates the buyer to honor its obligation to the seller.”

At issue is whether (and how) an entity should assess a buyer’s **continuing investment** for condominium unit sales during the period before the buyer and developer close the sale.

The Task Force reached a consensus in Issue 06-8 that an entity should evaluate the adequacy of the buyer’s continuing investment, pursuant to paragraph 12 of Statement 66, in determining whether to recognize profit under the percentage-of-completion method. The Task Force also reached a consensus that (1) the buyer’s initial and continuing investment tests should only consider nonrefundable amounts and (2) when an entity reassesses the criteria in paragraph 37 of Statement 66, the buyer’s initial and continuing investment tests should be applied prospectively on a reassessment date (i.e., as though the reassessment date were the initial contract date).

An entity can meet the continuing investment test by requiring the buyer to either (1) make additional payments during the construction term at least equal to the level **annual** payment to fund principle and interest on a customary amortizing mortgage for the remaining purchase price of the property or (2) increase the minimum initial investment, as defined in Statement 66, by an equivalent aggregate amount. As part of this assessment, the remaining purchase price should be determined on the basis of the sales price of the property. If the buyer’s initial or **continuing** investment is not sufficient, the developer should apply the deposit method.

EFFECTIVE: First annual reporting period beginning after March 15, 2007. Earlier application is permitted as of the beginning of a fiscal year.

TRANSITION: Apply as a change in accounting principle through a cumulative-effect adjustment at the beginning of the year of adoption.

Other SEC Matters

SEC Order Approving Proposed Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees and Notice of Filing and Order Granting Accelerated Approval of the Amendment Delaying Implementation of Certain of These Rules

AFFECTS: Public companies and their auditors.

SUMMARY: The SEC approved the PCAOB’s ethics and independence rules and technical amendments. The following chart briefly summarizes the rules and effective dates:

| Rule | Description | Effective Date |
|-------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3501 — Definition of Terms | Defines terms used in the rules | April 29, 2006 |
| 3502 — Responsibility Not to Knowingly or Recklessly Contribute to Violations | Codifies the principle that persons associated with a registered public accounting firm should not cause the firm to violate relevant laws, rules, and professional standards because of an act or omission that the person knew or should have known would directly and substantially contribute to such a violation | April 29, 2006 |
| 3520 — Auditor Independence | Articulates the foundation for current independence requirements | April 29, 2006 |
| 3521 — Contingent Fees | Prohibits contingent fee arrangements between a public accounting firm and its audit clients | Does not apply to contingent fee arrangements that before June 18, 2006, were (1) paid in their entirety, (2) converted to fixed fee arrangements, or (3) otherwise unwound |
| 3522 — Tax Transactions | Prohibits auditors from providing services to their audit clients related to the tax treatment of confidential transactions or aggressive tax position transactions | Does not apply to tax services that are completed by a registered public accounting firm before June 18, 2006 |
| 3523 — Tax Services for Persons in Financial Reporting Oversight Roles | Prohibits auditors from providing tax services to persons in a financial reporting oversight role at an audit client | Does not apply to tax services being provided pursuant to an engagement in process on April 19, 2006, provided those services are completed on or before October 31, 2006 (see further discussion below) |
| 3524 — Audit Committee Preapproval of Certain Tax Services | Requires auditors seeking preapproval of tax services to (1) provide the audit committee written documentation related to the scope of and fee for such services and (2) discuss potential effects on the firm's independence | Does not apply to any tax service preapproved on an engagement-by-engagement basis before June 18, 2006. With respect to tax services provided to audit clients whose audit committees preapprove tax services pursuant to policies and procedures, does not apply to any such tax service that is begun by April 20, 2007 |

The PCAOB is adjusting the implementation schedule for one part of Rule 3523. Currently, Rule 3523 prohibits auditors from providing tax services to persons in a financial reporting oversight role at an audit client during both the audit and professional engagement periods. The audit period is defined in the SEC's independence rules, Rule 3501(a)(iii)(1), as the period covered by any financial statements being audited or reviewed. Rule 3501(a)(iii)(2) defines the professional engagement period as the period starting when the accounting firm either begins the audit procedures or signs the initial engagement letter, and ending when the SEC has been notified that the client is no longer the firm's client. The PCAOB decided not to apply Rule 3523 to tax services provided on or before April 30, 2007 (an extension from the original October 31, 2006, date), when those services were performed during the audit period and completed before the professional engagement period begins.

Regarding tax services provided during the professional engagement period, Rule 3523 remains unchanged. Therefore, registered public accounting firms must comply with that aspect of Rule 3523 as of November 1, 2006.

OTHER RESOURCES: [PCAOB Release No. 2005-14, Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees](#);

PCAOB Release No. 2005-020, Technical Amendments to Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees;
PCAOB Release No. 2006-001, Implementation Schedule for Certain Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees; and
PCAOB Release No. 2006-006, Implementation Schedule for Certain Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees.

SAB 108 Guidance on Materiality

AFFECTS: SEC registrants and their auditors.

SUMMARY: SAB 108 does the following:

- States that registrants should use both a balance sheet (iron curtain) approach and an income statement (rollover) approach when quantifying and evaluating the materiality of a misstatement.⁸
- Contains guidance on correcting errors under the dual approach.
- Provides transition guidance on correcting errors existing in prior years.

If a registrant early adopts, previous interim reports need not be amended. However, any comparative interim information presented should be adjusted to reflect the cumulative-effect adjustment as of the beginning of the year of initial application.

Although the specific provisions of SAB 108 do not apply to nonpublic entities, the ASB or FASB may issue future guidance on assessing materiality for nonpublic entities. The FASB discussed this topic at its [December 19, 2006, meeting](#). Private companies that are considering becoming registrants should note that the cumulative-effect adjustment is not available to registrants whose initial registration statements are not effective on or before November 15, 2006.

In the initial year of application, the staff will not object if a registrant records a one-time cumulative-effect adjustment to correct misstatements in prior fiscal years, provided that the errors were not deemed material under the registrant's prior approach but are material under the SAB 108 approach. The effects of the initial application should be reflected in the carrying amounts of assets and liabilities as of the beginning of that fiscal year with the offsetting adjustment to the opening balance of retained earnings. Also, registrants should disclose the nature and amount of each error being corrected, when and how it arose, and that the errors had previously been considered immaterial.

EFFECTIVE: For annual financial statements covering the first fiscal year ending after November 15, 2006, with earlier application encouraged for any interim period of the first fiscal year ending after November 15, 2006, and filed after the publication of the SAB (September 13, 2006).

OTHER RESOURCES: Deloitte & Touche's [Heads Up](#) and [SEC Alert 06-2](#) on SAB 108.

SEC Issues Interpretive Release on Use of Client Commissions for Brokerage and Research Services

AFFECTS: Money managers.

SUMMARY: Interpretive Release 34-54165 clarifies that money managers may use client commissions only for eligible brokerage and research services, which are limited to advice, analyses, and reports under Section 28(e) of the Exchange Act. The Interpretive Release outlines a three-step process required when analyzing the eligibility of brokerage and research services under Section 28(e). The steps include an analysis of:

⁸ SEC Staff Accounting Bulletin Topic 1.M, "Materiality," is unchanged by SAB 108. SAB Topic 1.M indicates that quantifying and aggregating errors is only the beginning of an analysis of materiality and that both quantitative and qualitative factors must be considered in determining whether individual errors are material.

- The application of the eligibility requirements.
- The money manager's lawful and appropriate use of the items.
- The money manager's good-faith determination that the commissions paid are reasonable in light of the value of the services received.

EFFECTIVE: The effective date of the Interpretive Release was July 24, 2006; however, market participants can rely on prior SEC guidance for six months after publication.

Tender Offer Best-Price Rules Amended

AFFECTS: Public entities and their auditors.

SUMMARY: The SEC gave final approval to changes to its "best-price" rule concerning tender offers. Final Rule Release 34-54684 requires that the consideration paid to any security holder in a tender offer is the highest consideration paid to any other security holder in the offer. The amendments also make clear that compensation for services that might be paid to a shareholder does not count as part of the price paid for those shares.

OTHER RESOURCES: For additional information, see the December 2005 issue of [Accounting Roundup](#).

SEC Updates Current Accounting and Disclosure Issues Document

AFFECTS: Public companies and their auditors.

SUMMARY: The SEC published an updated version of *Current Accounting and Disclosure Issues in the Division of Corporation Finance*. The document, which is an update of the December 1, 2005, publication, captures the SEC's significant rule-making developments and current views on a variety of accounting and disclosure topics.

In addition to specific rules proposed or adopted by the SEC (and covered in previous issues of *Accounting Roundup*), the document includes the following topics, which have been added or revised since December 2005:

- Operating segments and goodwill impairment.
- Aggregation of operating segments.
- Disclosures of liabilities for unpaid claims and claim adjustment expenses and reinsurance recoverables on paid and unpaid claims.
- Adoption of a new accounting standard in an interim period.
- Disclosures regarding cash flows associated with discontinued operations and insurance proceeds in the statement of cash flows.
- Disclosures regarding loss contingencies in MD&A.
- Shortcut method of assessing hedge effectiveness.
- Financial statement presentation and disclosure under Statement 133.
- Use of Form S-8, Form 8-K, and Form 20-F by public shell companies.
- Electronic notifications of effectiveness.
- Classification and measurement of warrants and embedded conversion features.
- Disclosures of off-balance-sheet arrangements.

AICPA Hosts Annual Conference on SEC and PCAOB Developments

AFFECTS: All entities and their auditors.

SUMMARY: The AICPA hosted its 2006 National Conference on Current SEC and PCAOB Developments, featuring speeches by, and Q&A sessions with, members of the SEC, PCAOB, and other standard-setting

organizations. **The speakers' remarks provide insight into the current concerns and priorities of their organizations.** The Conference also serves as a forum in which regulators share information and express concerns in advance of the annual reporting season. The overarching theme of this year's conference was the quality of financial reporting and ways to reduce its complexity. Other key topics were:

- Transparency of financial reporting and disclosure.
- Internal control reporting by management and independent auditors.
- Convergence of international standards and U.S. GAAP.
- XBRL (eXtensible business reporting language) reporting.
- Stock option backdating.
- Quantifying errors under the rollover approach versus the iron-curtain approach as discussed in SAB 108.
- Technical accounting issues, including those involving business combinations, fair value (e.g., Statement 157), income taxes (Interpretation 48), and financial instruments (derivatives, share-based payment, revenue recognition, consolidation, earnings per share, materiality, pensions, and postretirement benefits).

OTHER RESOURCES: See Deloitte & Touche LLP's [Heads Up](#) covering the highlights of the AICPA's December 11–13, 2006, National Conference on SEC and PCAOB Developments.

Other Auditing

ASB Issues SAS 113, *Omnibus* — 2006

AFFECTS: Auditors and practitioners who perform attest engagements for nonissuers.

SUMMARY: The ASB issued SAS 113, which amends the following standards to conform them to previously issued standards:

- Certain general and reporting standards in SAS 95, by clarifying the terminology used to describe professional requirements imposed on auditors in the 10 standards.
- SAS 99, by providing a clear link between the auditor's consideration of fraud and the auditor's assessment of risk in SAS 109 and the auditor's procedures in response to those assessed risks in SAS 110.
- Certain SASs (1, 57, 59, 85, and 101) that refer to the "completion of fieldwork" as the date of the auditor's report to conform to changes made in SAS 103. SAS 103 requires that the date of the auditor's report not be prior to the date on which the auditor has obtained sufficient appropriate audit evidence. The *Omnibus* amends these SASs for the dating of both the auditor's report and the management representation letter.

EFFECTIVE: Certain parts of the statement (namely, the amendments in paragraphs 1–5) are effective for audits of financial statements for periods **beginning** on or after December 15, 2006. Paragraphs 7–14 of the statement are effective for audits of financial statements for periods **ending** on or after December 15, 2006. Earlier application is permitted for the entire statement.

ASB Issues SSAE 14, *SSAE Hierarchy*

AFFECTS: Auditors and practitioners who perform attest engagements for nonissuers.

SUMMARY: The ASB issued SSAE 14. The SSAE:

- Identifies the body of attest literature, establishing a hierarchy for publications.
- Clarifies the authority of attest publications issued by the AICPA and others.
- Specifies which attest publications the practitioner (1) must comply with and (2) should be aware of when conducting an attest engagement.

- Amends the 11 attestation standards to conform with the terms established in SSAE 13.

EFFECTIVE: SSAE 14 is effective when the subject matter or assertion is as of, or for, a period ending on or after December 15, 2006.

AICPA Professional Standards, ET Section 100.01, "Conceptual Framework for AICPA Independence Standards"

AFFECTS: Auditors of public and nonpublic companies.

SUMMARY: The "Conceptual Framework for AICPA Independence Standards" will require members to use a risk-based approach when determining whether a circumstance that is not addressed in the Code of Professional Conduct impairs a member's independence. The risk-based approach involves the following steps:

1. Identification and evaluation of threats to independence.
2. If, individually or in the aggregate, the threats are unacceptable (that is, they would compromise professional judgment), determination of whether identified threats are, or can be, eliminated or sufficiently mitigated by safeguards.
3. Determination of whether safeguards are available to eliminate unacceptable threats or reduce them to an acceptable level. If no such safeguards are available, independence is impaired.

EFFECTIVE: For all independence decisions made as of April 2007.

OTHER RESOURCES: [Issue No. 151 of AICPA News Update \(February 10, 2006\)](#).

Revision to AICPA Professional Standards, ET Section 501.02, "Response to Requests by Clients and Former Clients for Records"

AFFECTS: Auditors of public and nonpublic companies.

SUMMARY: The Revision addresses responses to requests by clients and former clients for records and requires that "client provided records" be returned to the client upon request, but that "client records prepared by the member" and other "supporting records" may be withheld if the engagement is incomplete or if fees due for the specific engagement are still outstanding.

EFFECTIVE: April 30, 2007.

OTHER RESOURCES: [Issue No. 151 of AICPA News Update \(February 10, 2006\)](#).

Guidance on Audit Reports for Nonissuers That Are a Subsidiary, Division, or Segment of an SEC Registrant

AFFECTS: Auditors of nonpublic subsidiaries, divisions, or segments of public companies.

SUMMARY: When the audited financial statements of a nonissuer subsidiary, division, or segment are included in the SEC filing of the parent, the auditing firm of the nonissuer subsidiary does not need to be registered with the PCAOB, unless it played a "significant role" in the audit of the SEC issuer. However, the audit of the nonissuer subsidiary must be performed in accordance with the auditing and related professional practice standards of the PCAOB.

AICPA Financial Reporting and Audit Risk Alerts

AFFECTS: All companies and auditors of public and nonpublic companies.

SUMMARY: The AICPA issued new and updated other Financial Reporting and Audit Risk Alerts for 2006. The new and updated alerts cover the following:

[Construction Contractors Accounting Developments \(new\)](#) — This Financial Reporting Alert supplements the AICPA's existing alert entitled *Construction Contractors Industry Developments*.

[Current Accounting Issues and Risks \(new\)](#) — This Financial Reporting Alert provides an overview of recent economic, industry, technical, and professional developments that affect financial reporting.

[SEC and PCAOB Developments \(new and later updated\)](#) — This Audit Risk Alert gives financial statement preparers and their auditors an overview of recent developments at the SEC and PCAOB regarding financial reporting and auditing matters.

[Understanding New Auditing Standards Relating to Risk Assessment \(new\)](#) — This Audit Risk Alert summarizes the requirements of the new AICPA risk assessment standards.

[Independence and Ethics Alert \(new\)](#) — This Audit Risk Alert provides AICPA members with guidance on recent developments in independence and ethics. Also included is guidance on performing nonattest services for attest clients and information about the independence rules and activities at the SEC, PCAOB, and GAO.

The AICPA also updated the [High-Technology Industry Developments](#), the [Real Estate Industry Developments](#), and the [Not-For-Profit Organizations Industry Developments](#) Audit Risk Alerts.

PCAOB Staff Q&As on Adjustments to Prior-Period Financial Statements Audited by a Predecessor Auditor

AFFECTS: Successor and predecessor auditors of public companies when there are adjustments to prior-period financial statements.

SUMMARY: Circumstances may arise that require an entity to make adjustments to prior-period financial statements, such as the reporting of discontinued operations, the retrospective application of a change in accounting principle, or the correction of an error in prior-period financial statements pursuant to Statement 154. The PCAOB has published staff Q&As addressing the auditing and reporting considerations of adjustments to prior-period financial statements when the prior periods have been audited by a predecessor auditor. The staff Q&As discuss situations from both the successor and predecessor auditors' perspectives.

Practice Aid on Auditing Alternative Investments

AFFECTS: Auditors and investors in alternative investments.

SUMMARY: Certain not-for-profit organizations, health-care entities, pension plans, and investment companies have increased their investment in financial instruments that do not have a readily determinable market value. Such investments (e.g., hedge funds, private equity funds, real estate funds) are known as "alternative investments" and are subject to fair value accounting. The investments expose investment portfolios to greater risk and volatility and inherently increase the risk of misstatement. As a result, the Audit Issues Task Force of the ASB established the Alternative Investments Task Force. The Task Force has developed and issued a non-authoritative practice aid to assist auditors in auditing alternative investments. The practice aid includes guidance on:

- General considerations pertaining to auditing alternative investments.
- Addressing management's financial statement existence and valuation assertions.
- Management representations.
- Disclosure of certain significant risks and uncertainties.
- Reporting.
- Confirmation for alternative investments.
- Due diligence, ongoing monitoring, and financial reporting controls.

AICPA TPAs on Effective Dates of a New SAS

AFFECTS: All entities required to apply SASs and their auditors.

SUMMARY: The AICPA issued two TPAs on determining the effective date of a new SAS. TIS Section 8100.01 discusses determining the effective date of a new SAS for audits of a single financial statement. The TPA states that a

new SAS would be effective for audits of an entity's single financial statement if the same SAS would be effective for audits of the entity's complete set of financial statements.

TIS Section 8100.02 discusses determining the effective date of a new SAS for audits of interim periods. This TPA uses examples to show that auditors should examine the entity's normal fiscal year to determine whether the SAS is effective.

GASB

Statement on Pollution Remediation Obligations

AFFECTS: State and local governmental entities.

SUMMARY: The GASB issued Statement 49, which requires governmental entities to estimate the components of expected pollution remediation costs and to record such costs as liabilities when any of the following five recognition triggers occur:

- Pollution poses an imminent danger to the public or environment and a government has little or no discretion to avoid fixing the problem.
- A government has violated a pollution-prevention-related permit or license.
- A regulator has identified (or evidence indicates it will identify) a government as responsible (or potentially responsible) for cleaning up pollution, or for paying all or some of the cost of the cleanup.
- A government is named (or evidence indicates that it will be named) in a lawsuit, compelling it to address the pollution.
- A government legally obligates itself to begin cleanup or post-cleanup activities (limited to activities the government is legally required to complete).

GASB Statement 49 requires that a governmental entity use an "expected cash flows" measurement technique to predict its expected outlays for pollution remediation obligations. The Statement applies to remediation activities, such as site assessment and cleanups of existing pollution. Pollution prevention or control obligations with respect to current operations, as well as future pollution remediation activities that are required upon retirement of an asset (e.g., landfill closure and post-closure care and power plant decommissioning), are excluded from the scope of the Statement.

GASB Statement 49 also requires governments to disclose information about their pollution obligations associated with cleanup efforts in the footnotes to their financial statements.

EFFECTIVE: The Statement is effective for financial statements for periods beginning after December 15, 2007.

TRANSITION: Liabilities should be measured at the beginning of the period of adoption so that beginning net assets can be restated.

Statement on Accounting for Sales and Pledges of Receivables and Future Revenues

AFFECTS: State and local governmental entities.

SUMMARY: Statement 48 clarifies the guidance on accounting for sales and pledges of receivables and future revenues. The Statement provides criteria that governments will use to determine whether to classify certain transactions as sold or collateralized. In other words, Statement 48 determines whether proceeds received from a certain transaction should be reported as revenue or a liability. The Statement also indicates that governments should not revalue assets that are transferred between financial reporting entity components. The Statement contains several modifications from the 2005 Exposure Draft and also does the following:

- Requires enhanced disclosures pertaining to future revenues that have been pledged or sold.

- Provides guidance on sales of receivables and future revenues within the same financial reporting entity.
- Provides guidance on recognizing other assets and liabilities arising from the sale of specific receivables or future revenues.

EFFECTIVE: Statement 48 is effective for financial statements for periods beginning after December 15, 2006.

New Q&A on Qualifying OPEB Plan Trusts and Fiduciary Responsibilities

AFFECTS: State and local governmental entities.

SUMMARY: The GASB issued a Q&A intended to provide implementation guidance regarding qualifying other postemployment benefit (OPEB) plan trusts and the responsibilities of those who play a significant role in the functions of an OPEB plan that includes such a trust, for purposes of accounting and financial reporting in accordance with the requirements of GASB Statements 43 and 45.

Because many governments are implementing the OPEB standards, the GASB released the Q&A ahead of schedule. The Q&A is also included in the [Comprehensive Implementation Guide — 2006](#)

International

IASB Issues Operating Segments Standard

AFFECTS: Listed entities that apply IFRSs.

SUMMARY: As part of the convergence project to align IFRSs and U.S. GAAP, the IASB released IFRS 8, a standard on segment reporting. IFRS 8 replaces IAS 14 and aligns segment reporting with the requirements of Statement 131.

IFRS 8 applies only to listed entities and requires identification of operating segments on the basis of internal reports that are regularly reviewed by the entity's chief operating decision maker in order to allocate resources to the segment and assess its performance (i.e., the "management approach"). Under IFRS 8, the definition of "operating segment" has been broadened to include a component of an entity that sells primarily or exclusively to other operating segments of the same entity if that entity is managed in this manner.

IFRS 8 requires explanations of how the segment information is prepared, as well as reconciliations of total reportable segment revenues, total profits or losses, total assets, total liabilities, and other amounts disclosed for reportable segments to corresponding amounts recognized in the entity's financial statements.

EFFECTIVE: IFRS 8 applies to the annual financial statements for periods beginning on or after January 1, 2009. Earlier application is permitted.

OTHER RESOURCES: For [more information](#), visit Deloitte's IAS Plus Web site.

IFRIC Interpretation on Service Concession Arrangements

AFFECTS: Service concession operators that apply IFRSs.

SUMMARY: The IFRIC issued IFRIC 12, an Interpretation that addresses how IFRSs are applied by service concession operators when accounting for the obligations they undertake and rights they receive in service concession arrangements.

In this guidance, the IASB discusses the accounting challenges posed by the large number of complex long-term arrangements that governments use with the private sector to discharge their public responsibilities. IFRIC 12 applies only to service concession operators and does not address accounting for the governmental aspect of service concession arrangements.

IFRIC 12 interprets the requirements of a number of relevant IFRSs, including those concerning accounting for construction contracts, service contract revenue, borrowing costs, financial assets, and intangible assets. Although IFRIC 12 outlines two types of service concession arrangements and deals with the respective accounting models (i.e., the Financial Asset Model and the Intangible Asset Model), the Interpretation also recognizes that both arrangement types may apply to a single contract.

EFFECTIVE: IFRIC 12 is effective for annual periods beginning on or after March 1, 2007. Earlier application is permitted.

OTHER RESOURCES: For [more information](#), visit Deloitte's IAS Plus Web site.

IFRIC Interpretation on Group and Treasury Share Transactions

AFFECTS: Entities that apply IFRSs.

SUMMARY: The IFRIC has issued IFRIC 11, an Interpretation that addresses the application of IFRS 2 to share-based payment arrangements in three circumstances:

- Share-based payments in which the entity chooses or is required to buy its own equity instruments to settle the share-based payment obligation should be accounted for as equity-settled share-based payment transactions.
- When a parent grants employees of a subsidiary rights to its equity instruments, assuming the transaction is recorded as an equity-settled transaction in the consolidated financial statements, the subsidiary would also record the transaction as an equity-settled transaction in its financial statements.
- When a subsidiary grants its employees rights to equity instruments of its parent, the subsidiary should record the transaction as a cash-settled share-based payment transaction.

EFFECTIVE: IFRIC 11 is effective for annual periods beginning on or after March 1, 2007. Earlier application is permitted.

OTHER RESOURCES: For [more information](#), visit Deloitte's IAS Plus Web site.

IFRIC Interpretation on Interim Financial Reporting and Impairment

AFFECTS: Companies that apply IFRSs.

SUMMARY: IFRIC Interpretation 10 addresses the potential conflict between requirements of IAS 34 and the requirements for recording impairment losses on goodwill in IAS 36 and certain financial assets in IAS 39. IAS 34 requires that entities assess goodwill for impairment at each reporting date and assess investments in equity instruments and financial assets carried at cost for impairment at every balance sheet date. Because these assessments should be performed at each reporting or balance sheet date, the results of the assessments in subsequent periods may indicate that an impairment loss previously recorded would not have existed if assessment had only occurred at the subsequent period. The question then becomes whether this impairment loss should be reversed at the subsequent period as IAS 34 suggests. IFRIC Interpretation 10 states that "an entity shall not reverse an impairment loss recognized in a previous interim period in respect of goodwill or an investment in either an equity instrument or a financial asset carried at cost."

EFFECTIVE: IFRIC Interpretation 10 is effective for annual periods beginning on or after November 1, 2006. Earlier application is encouraged, and disclosure of that fact is required.

TRANSITION: Requirements shall be applied prospectively.

IFRIC Interpretation 9, *Reassessment of Embedded Derivatives*

AFFECTS: Companies that apply IFRSs and enter into contracts that may contain embedded derivatives.

SUMMARY: IFRIC 9 clarifies certain aspects of the treatment of embedded derivatives under IAS 39 and states that an entity shall assess whether an embedded derivative is required to be bifurcated from the host contract and accounted for separately when an entity first becomes a party to the contract. Subsequent reassessments are prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract. In such cases, reassessment is required.

EFFECTIVE: For annual periods beginning on or after June 1, 2006.

TRANSITION: Retrospective application is required.

IFRIC Interpretation 8, *Scope of IFRS 2*

AFFECTS: Companies that apply IFRSs and issue share-based payments.

SUMMARY: IFRIC 8 clarifies that IFRS 2 applies to arrangements in which an entity makes share-based payments to employees and non-employees for consideration **that is less than the fair value** of the equity instrument granted or liability incurred. It also clarifies that this situation indicates that additional consideration has been or will be received. The identifiable consideration should be measured in accordance with IFRS 2, and the unidentifiable (i.e., additional) consideration should be measured as the difference between the fair value of the share-based payment and the fair value of the identifiable consideration received.

EFFECTIVE: For annual periods beginning on or after May 1, 2006.

TRANSITION: Retrospective application in accordance with the requirements of IAS 8, subject to the transitional provisions of IFRS 2.

Application of New IFRSs Not Effective Until 2009

AFFECTS: Companies that apply IFRSs or that will adopt, converge, or both, with IFRSs and standard setters.

SUMMARY: To help bring stability to an increasingly active IFRS environment, the IASB announced it will take steps to assist those involved with implementing IFRSs around the world. These steps include:

- Increased lead time to prepare for new standards.
- Increased opportunity for input on conceptual issues.
- Public roundtables on two key topics:
 1. Proposed amendments to the recognition and measurement principles in IAS 37.
 2. Measurement phase of the Conceptual Framework.

In addition, the IASB announced that it will not require the application of new IFRSs under development or major amendments to existing standards before January 1, 2009. However, this announcement does not preclude the issuance of new standards, or their early adoption, should a company choose that course. Also, interpretations and minor amendments as a result of implementation issues are not subject to this timeline. The 2009 implementation date will, however, apply to all major IASB projects.

Appendix A: Summary of SAB Topic 11.M

SEC Staff Accounting Bulletin Topic 11.M indicates that filings that include financial statements should include disclosure of the impact that a recently issued accounting standard will have on the financial position and results of operations of the registrant when such a standard is adopted in a future period. This disclosure guidance applies to all accounting standards that have been issued but not yet adopted by the registrant unless the impact on its financial position and results of operations is not expected to be material. MD&A requires disclosure of presently known material changes, trends, and uncertainties that have had, or that the registrant reasonably expects will have, a material impact on future sales, revenues, or income from continuing operations. With respect to financial statement disclosures, generally accepted auditing standards specifically address the need for the auditor to consider the adequacy of the disclosure of impending changes in accounting principles if (1) the financial statements have been prepared on the basis of accounting principles that were acceptable at the financial statement date but that will not be acceptable in the future and (2) the financial statements will be restated in the future as a result of the change. The SEC staff believes that recently issued accounting standards may constitute material matters and, therefore, that disclosure in the financial statements should also be considered when the change to the new accounting standard will be accounted for in financial statements of future periods, prospectively or with a cumulative catch-up adjustment.

Disclosures should include the following:

- A brief description of the new standard, the date that adoption is required, and the date that the registrant plans to adopt, if earlier.
- A discussion of the methods of adoption allowed by the standard and the method expected to be used by the registrant, if determined.
- A discussion of the impact that adoption of the standard is expected to have on the financial statements of the registrant, unless not known or not reasonably estimable, in which case a statement to that effect may be made.
- Disclosure of the potential impact of other significant matters that the registrant believes might result from the adoption of the standard (e.g., technical violations of debt covenant agreements, planned or intended changes in business practices) is encouraged.

Appendix B: Abbreviations

| | | | |
|--------------|----------------------------------------------------|-----------------|-------------------------------------------------------------|
| AcSEC | Accounting Standards Executive Committee | IAS | International Accounting Standard |
| AICPA | American Institute of Certified Public Accountants | IASB | International Accounting Standards Board |
| APB | Accounting Principles Board | IFAC | International Federation of Accountants |
| ARB | Accounting Research Bulletin | IFRIC | International Financial Reporting Interpretations Committee |
| ASB | Auditing Standards Board | IFRS | International Financial Reporting Standard |
| DIG | Derivatives Implementation Group | MD&A | Management's Discussion & Analysis |
| EITF | Emerging Issues Task Force | NCGA | National Council on Governmental Accounting |
| FAS | Financial Accounting Standard | PCAOB | Public Company Accounting Oversight Board |
| FASB | Financial Accounting Standards Board | SAB | Staff Accounting Bulletin |
| FIN | FASB Interpretation | SAS | Statement on Auditing Standards |
| FSP | FASB Staff Position | SEC | Securities and Exchange Commission |
| GAAP | Generally Accepted Accounting Principles | SOP | Statement of Position |
| GAO | Government Accountability Office | SSAE | Statement on Standards for Attestation Engagements |
| GASB | Governmental Accounting Standards Board | TPA | Technical Practice Aid |

Appendix C: Glossary of Standards

FASB Statement No. 5, *Accounting for Contingencies*

FASB Statement No. 13, *Accounting for Leases*

FASB Statement No. 43, *Accounting for Compensated Absences*

FASB Statement No. 66, *Accounting for Sales of Real Estate*

FASB Statement No. 87, *Employers' Accounting for Pensions*

FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*

FASB Statement No. 109, *Accounting for Income Taxes*

FASB Statement No. 116, *Accounting for Contributions Received and Contributions Made*

FASB Statement No. 123(R), *Share-Based Payment*

FASB Statement No. 126, *Exemption From Certain Required Disclosures About Financial Instruments for Certain Nonpublic Entities — an amendment of FASB Statement No. 107*

FASB Statement No. 131, *Disclosures About Segments of an Enterprise and Related Information*

FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*

FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*

FASB Statement No. 143, *Accounting for Asset Retirement Obligations*

FASB Statement No. 150, *Accounting for Certain Financial Instruments With Characteristics of Both Liabilities and Equity*

FASB Statement No. 154, *Accounting Changes and Error Corrections* — a replacement of APB Opinion No. 20 and FASB Statement No. 3

FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*

FASB Statement No. 156, *Accounting for Servicing of Financial Assets*

FASB Statement No. 157, *Fair Value Measurements*

FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* — an amendment of FASB Statements No. 87, 88, 106, and 132(R)

FASB Interpretation No. 14, *Reasonable Estimation of the Amount of a Loss*

FASB Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*

FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities* — an interpretation of ARB No. 51

FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations*

FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* — an interpretation of FASB Statement No. 109

FASB Staff Position No. FAS 13-2, "Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction"

FASB Staff Position No. FAS 123(R)-1, "Classification and Measurement of Freestanding Financial Instruments Originally Issued in Exchange for Employee Services Under FASB Statement No. 123(R)"

FASB Staff Position No. FAS 123(R)-5, "Amendment of FASB Staff Position FAS 123(R)-1"

FASB Staff Position No. FAS 123(R)-6, "Technical Corrections of FASB Statement No. 123(R)"

FASB Staff Position No. FAS 126-1, "Applicability of Certain Disclosure and Interim Reporting Requirements for Obligors for Conduit Debt Securities"

FASB Staff Position No. FIN 46(R)-6, "Determining the Variability to Be Considered in Applying FASB Interpretation No. 46(R)"

FASB Staff Position No. AUG AIR-1, "Accounting for Planned Major Maintenance Activities"

FASB Staff Position No. EITF 00-19-2, "Accounting for Registration Payment Arrangements"

FASB Staff Position No. FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors"

FASB Technical Bulletin No. 85-4, *Accounting for Purchases of Life Insurance*

FASB Concepts Statement No. 6, *Elements of Financial Statements*

EITF Issue No. 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments"

EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock"

EITF Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)"

EITF Issue No. 03-7, "Accounting for the Settlement of the Equity-Settled Portion of a Convertible Debt Instrument That Permits or Requires the Conversion Spread to Be Settled in Stock (Instrument C of Issue No. 90-19)"

EITF Issue No. 05-1, "Accounting for the Conversion of an Instrument That Becomes Convertible Upon the Issuer's Exercise of a Call Option"

EITF Issue No. 05-7, "Accounting for Modifications to Conversion Options Embedded in Debt Instruments and Related Issues"

EITF Issue No. 06-1, "Accounting for the Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service From the Service Provider"

EITF Issue No. 06-2, "Accounting for Sabbatical Leave and Other Similar Benefits Pursuant to FASB Statement No. 43, *Accounting for Compensated Absences*"

EITF Issue No. 06-3, "How Taxes Collected From Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross Versus Net Presentation)"

EITF Issue No. 06-4, "Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements"

EITF Issue No. 06-5, "Accounting for Purchases of Life Insurance — Determining the Amount That Could Be Realized in Accordance With FASB Technical Bulletin No. 85-4, *Accounting for Purchases of Life Insurance*"

EITF Issue No. 06-6, "Debtor's Accounting for a Modification (or Exchange) of Convertible Debt Instruments"

EITF Issue No. 06-7, "Issuer's Accounting for a Previously Bifurcated Conversion Option in a Convertible Debt Instrument When the Conversion Option No Longer Meets the Bifurcation Criteria in FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*"

EITF Issue No. 06-8, "Applicability of the Assessment of a Buyer's Continuing Investment Under FASB Statement No. 66, *Accounting for Sales of Real Estate*, for Sales of Condominiums"

EITF Issue No. 06-9, "Reporting a Change in (or Elimination of) a Previously Existing Difference Between the Fiscal Year-End of a Parent Company and That of a Consolidated Entity or Between the Reporting Period of an Investor and That of an Equity Method Investee"

EITF Topic No. D-98, "Classification and Measurement of Redeemable Securities"

Statement 133 Implementation Issue No. G19, "Cash Flow Hedges: Hedging Interest Rate Risk for the Forecasted Issuances of Fixed-Rate Debt Arising From a Rollover Strategy"

Statement 133 Implementation Issue No. G26, "Cash Flow Hedges: Hedging Interest Cash Flows on Variable-Rate Assets and Liabilities That Are Not Based on a Benchmark Interest Rate"

APB Opinion No. 12, *Omnibus Opinion — 1967*

APB Opinion No. 21, *Interest on Receivables and Payables*

APB Opinion No. 22, *Disclosures of Accounting Policies*

APB Opinion No. 25, *Accounting for Stock Issued to Employees*

APB Opinion No. 28, *Interim Financial Reporting*

GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*

GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pension Plans

GASB Statement No. 48, Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues

GASB Statement No. 49, Accounting and Financial Reporting for Pollution Remediation Obligations

AICPA Statement on Auditing Standards No. 1, Codification of Auditing Standards and Procedures

AICPA Statement on Auditing Standards No. 57 (AU Section 342), Auditing Accounting Estimates

AICPA Statement on Auditing Standards No. 59 (AU Section 341), The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern

AICPA Statement on Auditing Standards No. 60 (AU Section 325A), Communication of Internal Control Related Matters Noted in an Audit

AICPA Statement on Auditing Standards No. 85 (AU Section 333), Management Representations

AICPA Statement on Auditing Standards No. 95 (AU Section 150), Generally Accepted Auditing Standards

AICPA Statement on Auditing Standards No. 99 (AU Section 316), Consideration of Fraud in a Financial Statement Audit

AICPA Statement on Auditing Standards No. 101 (AU Section 328), Auditing Fair Value Measurements and Disclosures

AICPA Statement on Auditing Standards No. 103 (AU Section 339), Audit Documentation

AICPA Statement on Auditing Standards No. 109 (AU Section 314), Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement

AICPA Statement on Auditing Standards No. 110 (AU Section 318), Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained

AICPA Statement on Auditing Standards No. 112 (AU Section 325), Communicating Internal Control Related Matters Identified in an Audit

AICPA Statement on Auditing Standards No. 113 (AU Section 150), Omnibus — 2006

AICPA Statement of Position 01-4, Reporting Pursuant to the Association for Investment Management and Research Performance Presentation Standards

AICPA Statement of Position 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer

AICPA Statement of Position 06-1, Reporting Pursuant to the Global Investment Performance Standards

AICPA Professional Standards, AT Section 501, "Reporting on an Entity's Internal Control Over Financial Reporting"

AICPA Technical Practice Aids, TIS Section 5700.01, "Income Tax Accounting for Contributions to Certain Nonprofit Scholarship Funding Organizations"

AICPA Technical Practice Aids, TIS Section 8100.01, "Determining the Effective Date of a New Statement on Auditing Standards for Audits of a Single Financial Statement"

AICPA Technical Practice Aids, TIS Section 8100.02, "Determining the Effective Date of a New Statement of Auditing Standards for Audits of Interim Periods"

AICPA Center for Public Company Audit Firms Alert #90, SEC Staff Position Regarding Changes to the Statement of Cash Flows Relating to Discontinued Operations

AICPA Center for Public Company Audit Firms Alert #98, Update to SEC Staff Position Regarding Changes to the Statement of Cash Flows Relating to Discontinued Operations (Addendum to CPCAFA Alert #90)

SEC Staff Accounting Bulletin No. 107, codified as SAB Topic 14, "Share-Based Payment"

SEC Staff Accounting Bulletin No. 108, codified as SAB Topic 1.N, "Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements"

SEC Staff Accounting Bulletin Topic 11.M, "Disclosure of the Impact That Recently Issued Accounting Standards Will Have on the Financial Statements of the Registrant When Adopted in a Future Period"

SEC Final Rule Release No. 33-8713, Fund of Funds Investments

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| SEC Final Rule Release No. 33-8732A, <i>Executive Compensation and Related Person Disclosure</i> | IAS 8, <i>Accounting Policies, Changes in Accounting Estimates and Errors</i> |
| SEC Final Rule Release No. 33-8730A, <i>Internal Control Over Financial Reporting in Exchange Act Periodic Reports of Foreign Private Issuers That Are Accelerated Filers</i> | IAS 14, <i>Segment Reporting</i> |
| | IAS 34, <i>Interim Financial Reporting</i> |
| SEC Final Rule Release No. 33-8760, <i>Internal Control Over Financial Reporting in Exchange Act Periodic Reports of Non-Accelerated Filers and Newly Public Companies</i> | IAS 36, <i>Impairment of Assets</i> |
| | IAS 37, <i>Provisions, Contingent Liabilities and Contingent Assets</i> |
| SEC Final Rule Release No. 34-54684, <i>Amendments to the Tender Offer Best-Price Rules</i> | IAS 39, <i>Financial Instruments: Recognition and Measurement</i> |
| SEC Interim Final Rules Release No. 33-8765, <i>Executive Compensation Disclosure</i> | IFRS 2, <i>Share-Based Payment</i> |
| | IFRS 8, <i>Operating Segments</i> |
| SEC Accounting Series Release No. 268 (FRR Section 211), <i>Redeemable Preferred Stocks</i> | IFRIC Interpretation 8, <i>Scope of IFRS 2</i> |
| SEC Interpretive Release No. 34-54165, <i>Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934</i> | IFRIC Interpretation 9, <i>Reassessment of Embedded Derivatives</i> |
| ASB Statement on Standards for Attestation Engagements No. 13, <i>Defining Professional Requirements in Statements on Standards for Attestation Engagements</i> | IFRIC Interpretation 10, <i>Interim Financial Reporting and Impairment</i> |
| ASB Statement on Standards for Attestation Engagements No. 14, <i>SSAE Hierarchy</i> | IFRIC Interpretation 11, <i>Group and Treasury Share Transactions</i> |
| | IFRIC Interpretation 12, <i>Service Concession Arrangements</i> |
| PCAOB Auditing Standard No. 2, <i>An Audit of Internal Control Over Financial Reporting Performed in Conjunction With an Audit of Financial Statements</i> | |
| PCAOB Auditing Standard No. 4, <i>Reporting on Whether a Previously Reported Material Weakness Continues to Exist</i> | |
| PCAOB Staff Audit Practice Alert (APA) No. 1, <i>Matters Related to Timing and Accounting for Option Grants</i> | |

Appendix D: Significant Adoption Dates

The chart below illustrates significant adoption dates for the FASB, EITF, GASB, AICPA/AcSEC, PCAOB, and IASB/IFRIC pronouncements that are discussed within the publication. As a reminder, this publication only includes **final** guidance that was issued by the standard setters and regulators during **2006**. For a complete listing of significant adoption dates, including final guidance that was issued prior to 2006, see Appendix B in the December 2006 issue of *Accounting Roundup*.

| FASB | Status |
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| Statement 158, <i>Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans</i> — an amendment of FASB Statements No. 87, 88, 106, and 132(R) | Recognition of asset and liability related to funded status of a plan and disclosures: <ul style="list-style-type: none"> For entities with publicly traded equity securities, effective for fiscal years ending after December 15, 2006. For all other entities, effective for fiscal years ending after June 15, 2007. For all entities, change in measurement date is effective for fiscal years ending after December 15, 2008. |
| Statement 157, <i>Fair Value Measurements</i> | Effective for fiscal years beginning after November 15, 2007, and interim periods within those years. |
| Statement 156, <i>Accounting for Servicing of Financial Assets</i> — an amendment of FASB Statement No. 140 | Effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. |
| Statement 155, <i>Accounting for Certain Hybrid Financial Instruments</i> — an amendment of FASB Statements No. 133 and 140 | Effective for all financial instruments acquired, issued, or subject to a remeasurement (new basis) event occurring after the beginning of an entity's first fiscal year that begins after September 15, 2006. |
| Interpretation 48, <i>Accounting for Uncertainty in Income Taxes</i> — an interpretation of FASB Statement No. 109 | Effective for fiscal years beginning after December 15, 2006. |
| FSP EITF 00-19-2, "Accounting for Registration Payment Arrangements" | Effective immediately for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified subsequent to December 21, 2006. Otherwise, effective for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years. |
| FSP FAS 126-1, "Applicability of Certain Disclosure and Interim Reporting Requirements for Obligors for Conduit Debt Securities" | Effective for fiscal periods beginning after December 15, 2006. If an entity issues interim financial statements, the FSP shall be applied to the first interim period after the date of adoption. |
| FSP FAS 123(R)-6, "Technical Corrections of FASB Statement No. 123(R)" | Effective for the first reporting period beginning after October 20, 2006, or an earlier period for which financial statements have not yet been issued. |
| FSP FAS 123(R)-5, "Amendment of FASB Staff Position FAS 123(R)-1" | Effective for the first reporting period beginning after October 10, 2006, or an earlier period for which financial statements have not yet been issued. |
| FSP FAS 123(R)-4, "Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement Upon the Occurrence of a Contingent Event" | Effective upon initial adoption of Statement 123(R). For an entity that adopted Statement 123(R) before February 3, 2006, this FSP is effective for the first reporting period beginning after February 3, 2006. |
| FSP FAS 13-2, "Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction" | Effective for fiscal years beginning after December 15, 2006. |
| FSP FIN 46(R)-6, "Determining the Variability to Be Considered in Applying FASB Interpretation No. 46(R)" | Effective the first day of the first reporting period beginning after June 15, 2006. |

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| FSP AUG AIR-1, "Accounting for Planned Major Maintenance Activities" | Effective for first fiscal year beginning after December 15, 2006. |
| FSP FTB 85-4-1, "Accounting for Life Settlement Contracts by Third Party Investors" | Effective for fiscal years beginning after June 15, 2006. |
| Statement 133 Implementation Issue No. G26, "Cash Flow Hedges: Hedging Interest Cash Flows on Variable-Rate Assets and Liabilities That Are Not Based on a Benchmark Interest Rate" | Effective the first day of the first fiscal quarter beginning after January 8, 2007. |
| EITF | Status |
| Issue 06-9, "Reporting a Change in (or the Elimination of) a Previously Existing Difference Between the Fiscal Year-End of a Parent Company and That of a Consolidated Entity or Between the Reporting Period of an Investor and That of an Equity Method Investee" | Effective for changes occurring in interim or annual reporting periods beginning after November 29, 2006. |
| Issue 06-8, "Applicability of the Assessment of a Buyer's Continuing Investment Under FASB Statement No. 66, <i>Sales of Real Estate</i> , for Sales of Condominiums" | Effective for first annual reporting period beginning after March 15, 2007. |
| Issue 06-7, "Issuer's Accounting for a Previously Bifurcated Conversion Option in a Convertible Debt Instrument When the Conversion Option No Longer Meets the Bifurcation Criteria in FASB Statement No. 133, <i>Accounting for Derivative Instruments and Hedging Activities</i> " | Effective for interim and annual periods beginning after December 15, 2006. |
| Issue 06-6, "Debtor's Accounting for a Modification (or Exchange) of Convertible Debt Instruments" | Applies to modifications (or exchanges) occurring in interim or annual reporting periods beginning after November 29, 2006. |
| Issue 06-5, "Accounting for Purchases of Life Insurance — Determining the Amount That Could Be Realized in Accordance With FASB Technical Bulletin No. 85-4" | Effective for fiscal years beginning after December 15, 2006. |
| Issue 06-4, "Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements" | Effective for fiscal years beginning after December 15, 2007. |
| Issue 06-3, "How Taxes Collected From Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross Versus Net Presentation)" | Effective for financial statements for interim and annual periods beginning after December 15, 2006. |
| Issue 06-2, "Accounting for Sabbatical Leave and Other Similar Benefits Pursuant to FASB Statement No. 43" | Effective for fiscal years beginning after December 15, 2006. |
| Issue 06-1, "Accounting for Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service From the Service Provider" | Effective for fiscal years beginning after June 15, 2007. |
| Issue 05-1, "Accounting for the Conversion of an Instrument That Became Convertible Upon the Issuer's Exercise of a Call Option" | Effective for all conversions within the scope of the issue that result from the exercise of call options in interim or annual reporting periods beginning after June 28, 2006. |
| GASB | Status |
| Statement No. 49, <i>Accounting and Financial Reporting for Pollution Remediation Obligations</i> | Effective for financial statements for periods beginning after December 15, 2007. |
| Statement No. 48, <i>Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues</i> | Effective for financial statements for periods beginning after December 15, 2006. |

| AICPA/AcSEC | Status |
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| SOP 06-1, <i>Reporting Pursuant to the Global Investment Performance Standards</i> | Effective April 6, 2006. |
| SAS 113, <i>Omnibus — 2006</i> | <p>The amendments in paragraphs 1 through 5 of this SAS are effective for audits of financial statements for periods beginning on or after December 15, 2006.</p> <p>The amendments in paragraphs 7 through 14 of this SAS are effective for audits of financial statements for periods ending on or after December 15, 2006.</p> |
| SAS 112, <i>Communicating Internal Control Matters Identified in an Audit</i> | Effective for audits of financial statements for periods ending on or after December 15, 2006. |
| SAS 111, <i>Amendment to Statement on Auditing Standards No. 39, Audit Sampling</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SAS 110, <i>Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SAS 109, <i>Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SAS 108, <i>Planning and Supervision</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SAS 107, <i>Audit Risk and Materiality in Conducting an Audit</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SAS 106, <i>Audit Evidence</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SAS 105, <i>Amendment to Statement on Auditing Standards No. 95, Generally Accepted Auditing Standards</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SAS 104, <i>Amendment to Statement on Auditing Standards No. 1, Codification of Auditing Standards and Procedures ("Due Professional Care in the Performance of Work")</i> | Effective for audits of financial statements for periods beginning on or after December 15, 2006. |
| SSAE 14, <i>SSAE Hierarchy</i> | Effective when the subject matter or assertion is as of or for a period ending on or after December 15, 2006. |
| Conforming changes to AICPA Professional Standards, AT Section 501 — <i>Reporting on an Entity's Internal Control Over Financial Reporting</i> , resulting from SAS 112 | Effective when the subject matter or the assertion is as of or for the period ending on or after December 15, 2006. |
| <i>Professional Standards</i> , ET Section 100.01 — <i>Conceptual Framework for AICPA Independence Standards</i> | Effective for all independence decisions made as of April 30, 2007. |
| Revision to AICPA Professional Standards, ET Section 501.02 | Effective April 30, 2006. |
| Center for Public Company Audit Firms Alert #90, <i>SEC Staff Position Regarding Changes to the Statement of Cash Flows Relating to Discontinued Operations</i> | Effective February 15, 2006. Retrospective modifications to presentations of the cash flows pertaining to discontinued operations in the first periodic report filed subsequent to February 15, 2006, may be treated similarly to a change in accounting method with no reference to the correction of an error. Modifications in subsequent filings should be treated as a correction of an error. |

| Center for Public Company Audit Firms Alert #98, <i>Update to SEC Staff Position Regarding Changes to the Statement of Cash Flows Relating to Discontinued Operations</i> (Addendum to CCAAF Alert #90) | Effective April 19, 2006. |
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| SEC | Status |
| Final Rule, <i>Internal Control Over Financial Reporting in Exchange Act Periodic Reports of Non-Accelerated Filers and Newly Public Companies</i> | For non-accelerated filers, auditor's attestation report on internal control over financial reporting must be included with annual reports for fiscal years ending on or after December 15, 2008. Management's report is required for fiscal years ending on or after December 15, 2007. For a newly public company, the requirement to provide either a management assessment of internal control over financial reporting or an auditor attestation report will be effective when it files its second annual report with the SEC. |
| Final Rule, <i>Internal Control Over Financial Reporting in Exchange Act Periodic Reports of Foreign Private Issuers That Are Accelerated Filers</i> | For foreign private issuers that are accelerated filers (but not large accelerated filers), auditor's attestation report on internal control over financial reporting must be included with annual reports for fiscal years ending on or after July 15, 2007. Management's report is required for fiscal years ending on or after July 15, 2006. |
| Interim Final Rule, <i>Executive Compensation Disclosure</i> | Effective December 29, 2006. Comments received by January 21, 2007, will be considered in decisions to make revisions, if any. |
| Final Rule, <i>Executive Compensation and Related Person Disclosure</i> | In Forms 8-K, effective for triggering events that occur on or after November 7, 2006, in Forms 10-K and 10KSB for fiscal years ending on or after December 15, 2006, and in registration and proxy/information statements filed after December 15, 2006. |
| Final Rule, <i>Fund of Funds Investments</i> | Effective July 31, 2006. |
| Amendments to Forms N-1A, N-2, N-3, N-4, and N-6 | All new registration statements filed on the investment company forms and all post-effective amendments that are annual updates to effective registration statements on the investment company forms filed on or after January 2, 2007, must include the disclosure required by the form amendments. |
| Final Rule, <i>Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports</i> (an extension of compliance date) | Effective for fiscal years ending on or after November 15, 2004, for certain "accelerated filers." Effective for fiscal years ending on or after July 15, 2007, for "nonaccelerated filers," including foreign private issuers that are not accelerated filers. Effective for fiscal years ending on or after July 15, 2006, for foreign private issuers that are accelerated filers and file annual reports on Form 20-F or 40-F. |
| SAB 108 (on the process of quantifying financial statement misstatements) | Effective for annual financial statements covering the first fiscal year ending after November 15, 2006. |
| Request for Additional Comments on <i>Interpretive Release, Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934</i> | The Interpretive Release is effective July 24, 2006; market participants, however, can rely on prior SEC guidance for six months after publication. |
| PCAOB | Status |
| Auditing Standard No. 4, <i>Reporting on Whether a Previously Reported Material Weakness Continues to Exist</i> | Effective February 6, 2006. |
| Rule 3524, <i>Audit Committee Pre-approval of Certain Tax Services</i> | Rule will not apply to any tax service preapproved on an engagement-by-engagement basis before June 18, 2006. With respect to tax services provided to audit clients whose audit committees preapprove tax services pursuant to policies and procedures, the rule will not apply to any such tax service that is begun by April 20, 2007. |

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| Rule 3523, <i>Tax Services for Persons in Financial Reporting Oversight Roles</i> | Rule will not apply to tax services being provided during the professional engagement period pursuant to an engagement in process at April 19, 2006, provided that such services are completed on or before October 31, 2006. Rule will not apply to tax services being provided on or before April 30, 2007, provided that those services were performed during the audit period and completed prior to the beginning of the professional engagement period. |
| Rule 3522, <i>Tax Transactions</i> | Rule will not apply to tax services that are completed by a registered public accounting firm prior to June 18, 2006. |
| Rule 3521, <i>Contingent Fees</i> | Rule will not apply to contingent fee arrangements that prior to June 18, 2006, were (1) paid in their entirety, (2) converted to fixed fee arrangements, or (3) otherwise unwound. |
| Rule 3501, <i>Definitions of Terms Employed in Section 3, Part 5 of the Rules</i> ; Rule 3502, <i>Responsibility Not to Knowingly or Recklessly Contribute to Violations</i> ; Rule 3520, <i>Auditor Independence</i> | Effective April 29, 2006. |
| IASB/IFRIC | Status |
| IFRS 8, <i>Operating Segments</i> | Effective for annual periods beginning on or after January 1, 2009. |
| IFRIC Interpretation 12, <i>Service Concession Arrangements</i> | Effective for annual periods beginning on or after March 1, 2007. |
| IFRIC Interpretation 11, <i>Group and Treasury Share Transactions</i> | Effective for annual periods beginning on or after March 1, 2007. |
| IFRIC Interpretation 10, <i>Interim Financial Reporting and Impairment</i> | Effective for annual periods beginning on or after November 1, 2006. |
| IFRIC Interpretation 9, <i>Reassessment of Embedded Derivatives</i> | Effective for annual periods beginning on or after June 1, 2006. |
| IFRIC Interpretation 8, <i>Scope of IFRS 2</i> | Effective for annual periods beginning on or after May 1, 2006. |

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