FASB/IASB UPDATE

- 2010 AAPA Port Finance Seminar
- Norfolk Virginia
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Outline

Codification

IFRS

- Convergence
- SEC Roadmap
- Private company (SME) reporting

Proposed standards

Codification

- Went live as US GAAP on 7/1/2009
- Numerous updates since that time
  - 17 in 2009 (after the 7/1 implementation date)
  - 18 in 2010 as of May 30

No. 168: *The* FASB Accounting Standards Codification™ *and the Hierarchy of Generally Accepted Accounting*

- Resources available
  - An online tutorial available on the Codification website at http://asc.fasb.org
  - A Notice to Constituents that includes a significant amount of background information at http://asc.fasb.org
  - A Codification Question and Answer (Q&A) document at http://www.fasb.org/cod_project/Cod_overview_12-08.pdf
  - Various webcasts http://www.fasb.org/fasb_webcast_series/index.shtml

No. 168: *The* FASB Accounting Standards Codification™ *and the Hierarchy of Generally Accepted Accounting*

- Resources available
  - Countdown to Codification Alerts, http://www.fasb.org/cs/ContentServer?c=Page&pagename=FASB%2FPage%2FSectionPage&cid=1176155830152
  - Details about the availability of the Codification, including subscription information and a planned print edition, are available at http://www.fasb.org/cs/ContentServer?c=Page&pagename=FASB%2FPage%2FSectionPage&cid=1176156264264

Codification

- More significant Update titles (2009)
  - *Fair Value Measurements and Disclosures (Topic 820)—Measuring Liabilities at Fair Value*
  - *Income Taxes (Topic 740)—Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*
  - *Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*
  - *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements*

Codification

- More significant Update titles (2009)
  - *Software (Topic 985): Certain Revenue Arrangements That Include Software Elements*
  - *Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance or Other Financing*
  - *Transfers and Servicing (Topic 860): Accounting for Transfers of Financial Assets*
  - *Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*

Codification

- Update titles (2010)
  - *Equity (Topic 505): Accounting for Distributions to Shareholders with Components of Stock and Cash*
  - *Consolidation (Topic 810): Accounting and Reporting for Decreases in Ownership of a Subsidiary—a Scope Clarification*
  - *Extractive Activities—Oil and Gas (Topic 932): Oil and Gas Reserve Estimation and Disclosures*
  - *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*

Codification

- Update titles (2010)
  - *Not-for-Profit Entities (Topic 958): Not-for-Profit Entities: Mergers and Acquisitions*
  - *Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements*
  - *Consolidation (Topic 810): Amendments for Certain Investment Funds*
  - *Derivatives and Hedging (Topic 815): Scope Exception Related to Embedded Credit Derivatives*

Codification

- Update titles (2010)
  - *Compensation—Stock Compensation (Topic 718): Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Currency of the Market in Which the Underlying Equity Security Trades*
  - *Financial Services—Insurance (Topic 944): How Investments Held through Separate Accounts Affect an Insurer's Consolidation Analysis of Those Investments*
  - *Entertainment—Casinos (Topic 924): Accruals for Casino Jackpot Liabilities*

Codification

- Update titles (2010)
  - *Revenue Recognition—Milestone Method (Topic 605): Milestone Method of Revenue Recognition*
  - *Receivables (Topic 310): Effect of a Loan Modification When the Loan Is Part of a Pool That Is Accounted for as a Single Asset*

Proposed Accounting Standards Updates

- Proposals in 2010:
  - Proposed Accounting Standards Update—*Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities—Financial Instruments (Topic 825) and Derivatives and Hedging (Topic 815)*
  - Proposed Accounting Standards Update—*Health Care Entities (Topic 954): Measuring Charity for Disclosure*
  - Proposed Accounting Standards Update—*Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries*

Proposed Accounting Standards Updates

- Proposals in 2010
  - Proposed Accounting Standards Update—*Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts*
  - Proposed Concepts Statement, *Conceptual Framework for Financial Reporting: The Reporting Entity*
  - Proposed Accounting Standards Update—*Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts*

Conceptual framework

- Proposed statement issued jointly with IASB
  - 3/11/2010
  - Comments due by 7/16/2010
- Likely to be elevated to authoritative status
- Entity concept
- Concept of control – consolidation required if an entity is controlled
  - Specifics of what constitutes control is left to the standards

IFRS

- SEC Roadmap
  - – No longer needs 20F reconciliation (2007)
  - – Voluntary use of IFRS by US registrants in 2010. Limited number of firms.
  - – Mandatory use phased in 2014/2015/2016
  - – Reassess whether to continue in 2011
- New SEC scuttlebut:
  - – Encourage convergence will reassess in 2011
  - – Closest time anyone is now talking about is 2016

IFRS

- Convergence
  - May 26, 2010: Delayed until the end of 2011
- Major areas to converge
  - Financial statement presentation
  - Leases
  - Revenue recognition
  - Financial instruments with characteristics of equity
  - Accounting for financial instruments

IFRS

- Major areas to converge (continued)
  - Consolidation: Policy and procedures
  - Insurance contracts
  - Statement of comprehensive income
  - Reporting discontinued operations
  - Balance sheet offsetting
  - Fair value measurement (due Q4 2010)
  - Emissions trading schemes (due date TBA)

IFRS

- Private Company Accounting (IFRS for SMEs)
- Simplified accounting for companies with no public reporting requirements
- Single stand alone standard
- AICPA allowable standard to audit against
- Less than 250 pages

Proposed Guidance

Conceptual Framework

Conceptual framework

- Qualitative Characteristics:
  - Relevance (predictive, feedback) nothing about timeliness
  - Faithful representation (complete, neutral, free from material error) nothing about verifiability
- Enhancing characteristics (comparability, verifiability [implies that different knowledgeable and independent observers could reach general consensus on how to report], timeliness, understandability)
- Constraints (cost, materiality)

Conceptual framework

- Definitions
  - Asset: An asset of an entity is a present economic resource to which the entity, through an enforceable right or other means, has access or can limit the access of others
  - Liability: A liability of an entity is a present economic obligation that is enforceable against the entity
  - Equity: Under discussion

Financial Statement Presentation

Financial Statement Presentation

- Proposed Sections
  - *Business* further broken down into Operating and Investing categories
  - *Financing* further broken down into Financing Asset and Financing Liability categories
  - *Income Taxes*
  - *Discontinued Operations*
  - *Equity* (Note: No Extraordinary Items Section)
- Primary perspective: Distinguishing between an entity's "value creating" (business) and "funding" (financing and equity) activities

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Financial Statement Presentation

- Cohesiveness is the governing principle
- Classification of assets and liabilities drives classification of changes in those items in
  - The statement of comprehensive income
  - The statement of cash flows
- Classification based on how an entity manages its business
  - Explain, as a matter of accounting policy, basis for classifying assets and liabilities
- Benefit: Clarifies relationships among financial statements' line items; facilitating financial analysis

Financial Statement Presentation

- Cash flow statement
  - Direct method required
  - Reconciliation of net income to cash flow from operations also required
- Single statement of Comprehensive Income

Financial Statement Presentation

Statement of Financial Position	Statement of Comprehensive Income	Statement of Cash Flows
Business **•Operating assets and liabilities** **•Investing assets and liabilities**	***Business*** **•Operating income and expenses** **•Investing income and expenses**	***Business*** **•Operating cash flows** **•Investing cash flows**
Financing **•Financing assets** **•Financing liabilities**	***Financing*** **•Financing asset income** **•Financing liability expenses**	***Financing*** **•Financing asset cash flows** **•Financing liability cash flows**
Income taxes	***Income taxes***	***Income taxes***
Discontinued operations	***Discontinued operations net of tax***	***Discontinued operations***
Equity	**OCI net of tax**	**Equity**

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Lessee Accounting

Lessee Accounting

- Convergence project with IASB
- Discussion paper comment period ended 7/17/2009
- The right to use is to be considered an asset (note the new conceptual framework matches this definition)
- Obligation to pay rentals is a liability

Lessee Accounting

- Whether a purchase option will be exercised will be reassessed each reporting period date. Changes the reassessment makes in the obligation to pay is recognized as an adjustment to the carrying amount of the right-to-use asset

- Obligation to pay includes contingent rentals remeasured each reporting date

Lessee Accounting

- Initial measurement
  - Liability valued using a discounted cash flow approach (approximates fair value)
  - Discounted using lessee's incremental borrowing rate
  - Initial asset measured at cost (discounted cash flow)
- Subsequent measurement
  - Liability at amortized cost (discount rate not reassessed)
  - Right to use asset at amortized cost

Lessee Accounting

- Changes in estimated lease payments
  - Catch up approach (bring up to date for the changes using the original discount rate)
- Impairment: not yet determined

Lessee Accounting

- Options to extend or terminate the lease, or purchase
  - A recognition issue rather than a measurement issue
  - Recognize the most likely lease term option, (IFRS probability weighted expected value)
  - Consider contractual, non-contractual and business factors
  - additional disclosure to allow users to differentiate
  - Lease term reassessment each reporting date on the basis of any new facts or circumstances
  - Change in liability recognized as an adjustment to the right-to-use asset

Lessee Accounting

- Contingent rentals and residual value guarantees
  – Most likely outcome (IFRS expected, probability weighted)
  – Remeasured at financial statement date through profit and loss (IFRS adjust the asset account)

- Residual value guarantees
  – Most likely outcome (IFRS expected, probability weighted)
  – Remeasured at financial statement date through profit and loss (IFRS adjust the asset account)

Lessee Accounting

- Presentation
  - Separate presentation of right-to-use assets (IFRS will not require separate presentation)
  - Presented based on classification of the underlying asset
  - Income statement presentation: depreciation, amortization, interest expense

Revenue Recognition

Revenue Recognition

- Applies to contracts with customers
  - Contract is an enforceable obligation (written or oral, explicit or implicit)
  - Customer is a party who contracts to obtain an asset from the entity’s ordinary activities
- Some possible scope exclusions
  - Derivitives
  - Insurance contracts
  - Lessor accounting for leases

Revenue Recognition

- Revenue recognized on the basis of increases in an entity's net position in a contract with a customer
  - Occurs when an entity performs by satisfying an obligation in the contract
  - Account for each obligation separately if transferred to the customer at different times
  - Revenue represents the transfer of assets to the customer

Revenue Recognition

- Satisfaction of a performance obligation
  - Asset transferred when customer obtains control of the underlying asset
  - Goods this is typically physical possession
  - Services when customer receives the contracted services
  - Activities are revenue ONLY IF they simultaneously transfer assets to the customer
  - Performance by customer does not lead to revenue recognition by the entity

Revenue Recognition

- Satisfaction of a performance obligation
  - Customer acceptance can affect when an asset is transferred to the customer
  - Customer control of an asset rather than the customer’s ability to use the asset as intended is the transfer point
  - Goods are generally transferred at a point in time while services may be continuously transferred

Revenue Recognition

- Measurement
  - Initially measured at transaction price
  - Subsequent measurement is entity's obligation to transfer goods and services
  - Revenue recognized is the amount of the transaction price allocated, at contract inception, to the satisfied performance obligations
  - This is not updated unless the contract is deemed onerous
  - Deemed onerous when costs exceed revenue-revise up to costs through profit and loss

Revenue Recognition

- Effects on current practice
  - Increases in inventory in absence of a contract is not revenue (agriculture, extractive industries)
  - Increases in inventory under a contract not yet transferred to a customer is not revenue (construction)
  - Warranties and sales incentives are deliverables requiring separate revenue recognition (not cost accruals)
  - Estimates must be used, based on stand alone selling prices (this counters EITF 00-21 and AICPA SOP 97-2)
  - Cost of obtaining contracts are expensed unless they qualify specifically under a different standard

Financial Instruments with Characteristics of Equity

Financial Instruments with Characteristics of Equity

- Issued November 2007 but still under deliberations
- Basic Ownership model
- Characteristics of Equity
  - A claim to a share of the assets in liquidation that have no priority over any other claim
  - Is entitled to a percentage of the assets that remain after all higher priority claims have been satisfied
  - Has no upper or lower limit

Financial Instruments with Characteristics of Equity

- Not Equity
  - Perpetual instruments (e.g., some preferred stock)
  - Senior classes of common stock
  - Limited partnership interest
  - Redeemable instruments (other than at fair value)
  - All equity derivatives (regardless of settlement provisions)

Financial Instruments with Characteristics of Equity

- Exceptions – redeemable instruments
  - Perpetual redeemable instruments equity if
    - Redemption amount equals share of net assets in liquidation
    - Redemption doesn’t impair the claims of higher priority instruments
  - Includes mandatorily or at the option of the holder and at fair value or an approximations of fair value

Financial Instruments with Characteristics of Equity

- Impact on balance sheet
  - More items classified as liabilities
  - Entities will appear significantly more leveraged
  - Debt covenants may need to be renegotiated
  - More instruments that need to be fair valued

Financial Instruments with Characteristics of Equity

- Impact on income sheet
  - Dividends on preferred stock expenses through earnings (reduced net income)
  - More contracts fair valued through earnings (potentially increased volatility in net income)
  - Gains on some contracts as value of liability decreases
  - Decrease demand for derivatives indexed to common shares

Financial Instruments with Characteristics of Equity

- Impact on Financial Analysis
  - Leveraged debt-equity ratios
  - Potentially more volatile performance measures
  - Subjectivity in determining fair values

Financial Instruments

Financial Instruments

- Most financial instruments at fair value
- Amortized cost also relevant and also presented
- Derivatives and trading financial instruments fair valued through income
- Instruments held for collection or payment:
  - reconcile fair value to amortized cost
  - If according to business strategy change in fair value through OCI with changes from interest accruals, credit impairment and realized gains and losses in net income

Financial Instruments

- Many financial liabilities of financial institutions kept at fair value
- Derivatives only need a qualitative assessment of hedging effectiveness makes hedging easier to qualify for
- Eliminates short cut method and critical terms match method
- Discontinue hedging only if criteria no longer met

QUESTIONS?

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FAS No. 164: *Not-for-Profit Entities: Mergers and Acquisitions*

- Determines whether a combination is a merger or an acquisition
- Applies the carryover method in accounting for a merger
- Applies the acquisition method in accounting for an acquisition, including determining which of the combining entities is the acquirer
- Determines what information to disclose to enable users of financial statements to evaluate the nature and financial effects of a merger or an acquisition.

No. 164: *Not-for-Profit Entities: Mergers and Acquisitions*

- This Statement is effective for: Mergers and acquisitions for which the merger/acquisition date is on or after the beginning of an initial reporting period beginning on or after December 15, 2009. It may not be applied to mergers or acquisitions before those dates.

No. 164: *Not-for-Profit Entities: Mergers and Acquisitions*

- Also effective prospectively for Not-for-profit entities for fiscal years starting on or after 12/15/2009
  - Statement 142's requirements on subsequent accounting for goodwill and other intangible assets acquired in an acquisition by a not-for-profit entity (Statement 142 refers to assets acquired in a *business combination*.)
  - The amendments that FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements,* made to Accounting Research Bulletin ARB No. 51, *Consolidated Financial Statements,* and to other existing pronouncements
  - The amendments that FASB Statement No. 141 (revised 2007), Business Combinations, made to existing pronouncements.

No. 164: *Not-for-Profit Entities: Mergers and Acquisitions*

- This Statement does not apply to:
  - The formation of a joint venture
  - The acquisition of an asset or a group of assets that does not constitute either a business or a nonprofit activity
  - A combination between not-for-profit entities, businesses, or nonprofit activities under common control
  - A transaction or other event in which a not-for-profit entity obtains control of another entity but does not consolidate that entity, as permitted or required by AICPA Statement of Position 94-3, *Reporting of Related Entities by Not-for-Profit Organizations,* or AICPA Audit and Accounting Guide, *Health Care Organizations.*

No. 164: *Not-for-Profit Entities: Mergers and Acquisitions*

- Applying Carryover method
  - Done at measurement date when the combination is effective not at the beginning of the period
  - Carried at book value with exceptions made to reflect consistent methods of accounting for the new entity if the merging entities used different methods and for the effects of intra-entity transactions
  - Effectively new entity accounting at point of merger
  - Carry forward in opening balances items such as hedge accounting requirements unless: 1. The merger results in a modification of a contract in a manner that would change those previous classifications or designations. 2. Reclassifications are necessary to conform accounting policies

No. 164: *Not-for-Profit Entities: Mergers and Acquisitions*

- Applying the acquisition method
  - Starts with FAS 141R and adjusts for non-profit specifics
  - Not-for-profits primarily supported by contributions and investment earnings should write off as a separate charge in the current periods what would otherwise be classified as goodwill asset
  - Provides guidance on the measurement and presentation of non-controlling interest (FAS 160 base)
  - Provides exceptions to the recognition principle for donor relationships, collections and conditional promises to give

No. 164: *Not-for-Profit Entities: Mergers and Acquisitions*

- Applying the acquisition method
  - Provides guidance on how to present in the statement of activities and the statement of cash flows things like: inherent contribution received, specific items that are to be with the performance indicator in the health care guide.
  - Includes minimum disclosure requirements tailored to not-for-profit entities

Accounting Standards Update

- No. 2009-06
- Income Taxes (Topic 740)
- Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities
  - Clarify when tax is attributable to the entity or to the owners
  - Determination of taxable status is a tax position
  - Reduced disclosure requirements for non-public entities