



# Accounting Roundup — Special Edition

## The Tidal Wave of Accounting and Financial Reporting Changes

May 2010



# A Compendium of the FASB's Joint and Individual Projects

by Deloitte & Touche LLP's Accounting Standards and Communications Group

Much of the recent debate in the financial reporting community has focused on when and if U.S.-based public entities should be permitted or required to adopt International Financial Reporting Standards (IFRSs) as a basis of reporting. The U.S. Securities and Exchange Commission (SEC) is expected to decide on the use of IFRSs for U.S. public entities sometime next year. In the meantime, the Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) have been working both individually and jointly on a number of projects that, if finalized, would bring about a seismic shift in the accounting and financial reporting landscape, the likes of which U.S. entities have never before experienced.

The FASB and IASB have been working both individually and jointly on a number of projects that, if finalized, would bring about a seismic shift in the accounting and financial reporting landscape.

While the FASB and IASB have been working together for over a decade, their more recent collaborative efforts have been under the auspices of a "Memorandum of Understanding" (originally the Norwalk Agreement that was signed in 2002). Recently, the two boards committed to expediting many of the joint projects in an effort to complete them by mid-2011. So, regardless of whether the SEC sets a date for U.S.-based public entities to convert to IFRSs, all U.S.-based entities will be affected by the changes to U.S. GAAP as a result of these efforts.

While the FASB and IASB are working jointly on a number of these projects, the focus of this special edition of *Accounting Roundup* is on the FASB's activities and the decisions that it has reached to date. These activities and the resulting changes to U.S. GAAP will affect U.S.-based entities the most in the short term. In addition, this special edition focuses on the projects with the broadest applicability and potential impact on financial reporting. It is not intended to be a "deep dive" into each of those projects; rather, it is meant to highlight some of the key changes the projects would make. Not interested in reading the thousands (yes, we said thousands) of pages of new accounting guidance? Well, in our customary fashion, we will issue a *Heads Up* article on each of these projects as they are exposed for public comment and again as they become final standards. The *Heads Up* articles provide that deeper dive into each of the proposed standards. Not a subscriber to our *Heads Up* articles? Follow this [link](#) to sign up.

This special edition does not address effective dates, since the joint projects that are discussed herein will be the subject of a comprehensive decision to either (1) set the effective date as the same date for all joint projects (what some have termed the "Big Bang") or (2) set separate effective dates for each respective project. The FASB and IASB plan to issue a discussion paper that lays out these two alternatives and seeks input from the boards' various constituent groups.

# Table of Contents and Timeline of FASB's Major Projects

	Expected Date					Page Number
	2Q	2010 3Q	4Q	2011 1H	2H	
<b>Joint FASB/IASB Projects</b>						1
Presentation of Financial Statements						1
Financial Statement Presentation	E	R		F		1
Discontinued Operations	E					2
Other Comprehensive Income	E			F		2
Financial Instruments						2
Accounting for Financial Instruments	E	R		F		2
Offsetting		E		F		3
Financial Instruments With Characteristics of Equity	E	R		F		4
Leases	E	R		F		4
Revenue Recognition	E	R		F		5
Consolidations	E	R		F		6
Fair Value Measurements	E	R	F			7
<b>FASB-Only Projects</b>						7
Disclosure of Certain Loss Contingencies	E	F				7
Going Concern	E	F				8
<b>Key Takeaways</b>						9

**E Exposure Draft**

**F Final Document**

**R Roundtable Discussion**

# Joint FASB/IASB Projects

## Presentation of Financial Statements

### *Financial Statement Presentation*

**Affects:** Most entities.<sup>1</sup>

**Summary:** In this project, the boards are taking a “fresh look” at the manner in which financial information is presented in an entity’s statement of financial position, statement of comprehensive income, and statement of cash flows. The revised financial statement format is expected to be more cohesive and split between business (i.e., operating and investing) and financing activities. This format would largely resemble the current presentation in the statement of cash flows. The intent of requiring a single financial statement presentation is to enhance the usefulness of financial information and increase the comparability and consistency of financial statements within and across entities. Specific changes would include the following:

- *Statement of financial position* — Requiring presentation of assets and liabilities by major activity within operating, investing, and financing categories.
- *Statement of comprehensive income* — Requiring a single statement of comprehensive income grouped by using the same categories as those in the statement of financial position; further disaggregation of line items in the statement would be required.
- *Statement of cash flows* — Requiring separate presentation of the main categories of cash receipts and cash payments for operating activities (i.e., direct method) rather than reconciliation of net income to net operating cash flows (i.e., indirect method). However, a reconciliation of operating income to net operating cash flows would be required in the notes to the financial statements.
- *Notes to the financial statements* — Requiring disclosure of the rationale used to classify assets and liabilities into categories and sections in the statement of financial position. In addition, an entity would be required to provide a reconciliation of beginning to ending balances of select assets and liabilities that management deems to be important to understanding the entity’s financial position.

**Consideration Points:** As a result of the revised financial statement presentation, entities may need to reassess their financial reporting processes to evaluate the manner in which they will adhere to these new requirements, particularly the shift to the direct method of presenting cash flows. This assessment could include an evaluation of the information technology systems or other processes used to gather financial statement information, the internal controls over the financial reporting process, and the resources within the financial reporting function for implementing necessary changes. Further, the proposed standard would most likely require entities to disaggregate their financial information and provide disclosures beyond what entities currently present in their financial statements. Thus, entities may need to evaluate (1) the effect of having to provide this additional financial information (e.g., the time it takes to identify, gather, and prepare the financial statements) and (2) how financial statement users analyze the information.

**Other Resources:** The FASB expects to issue an exposure draft of a proposed Accounting Standards Update (ASU) in the second quarter of 2010. The FASB staff expects to conduct roundtables during the third quarter of 2010. The Board expects to begin redeliberating the proposed ASU in the fourth quarter of 2010 and plans to issue a final ASU during the first half of 2011. ●

### *Discontinued Operations*

**Affects:** Entities disposing of a component of their operations.

**Summary:** The FASB is proposing to redefine a discontinued operation and the related disclosures. Tentatively, the FASB has agreed to a set of criteria that would converge with the current definition in IFRS 5.<sup>2</sup> Under the proposed guidance, a discontinued operation would be either:

- A component of an entity that either has been disposed of or is classified as held for sale and that represents (or is part of a single coordinated plan to dispose of) a separate major line of business or geographical area of operations.

<sup>1</sup> The proposed standard would not apply to the structure and content of general-purpose financial statements prepared by a not-for-profit entity or benefit plan within the scope of FASB Accounting Standard Codification Topics 960, *Plan Accounting — Defined Benefit Pension Plans*; 962, *Plan Accounting — Defined Contribution Pension Plans*; and 965, *Plan Accounting — Health and Welfare Benefit Plans*. Further, certain provisions would not apply to nonpublic entities, certain investment companies, common trust funds, variable annuity accounts, or similar funds that meet specific requirements.

<sup>2</sup> IFRS 5, *Non-current Assets Held for Sale*.

- A business that, on acquisition, meets the criteria for classification as held for sale.

The FASB expects the proposed guidance to result in fewer disposals that meet the criteria for classification as a discontinued operation on the face of the statement of comprehensive income. Therefore, to address concerns about the loss of information, the proposed guidance also includes expanded disclosure requirements both for discontinued operations and for significant components disposed of or to be disposed of that do not meet the revised criteria for classification as a discontinued operation.

The proposed guidance would also align the scope of ASC 205-20<sup>3</sup> with that of IFRS 5 to apply to all recognized noncurrent assets and to all disposal groups of an entity. The FASB expects the changes in scope to have a limited impact on entities, except for an entity's disposals of certain equity method investments, which could now qualify as a discontinued operation.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. ●

## *Other Comprehensive Income*

**Affects:** All entities, except those that have no other comprehensive income in any period presented or not-for-profit entities that are required to follow the guidance in ASC 958-205.<sup>4</sup>

**Summary:** Under current U.S. GAAP, entities can choose between several alternatives for displaying other comprehensive income and its components in the financial statements. The proposed ASU would eliminate those choices and would require entities to present comprehensive income in one continuous statement that displays net income and the components of other comprehensive income. However, the proposal would not change the calculation of earnings per share. That is, the control number for calculating EPS would still be net income available to common shareholders.

The proposed ASU would not change the items that must be reported in other comprehensive income. It also would not change the option for a preparer to show components of comprehensive income net of the effect of income taxes, as long as the preparer shows the tax effect for each component in the notes to the financial statements or on the face of the statement of comprehensive income.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. The Board's goal is to issue a final ASU in the first half of 2011. ●

## Financial Instruments

### *Accounting for Financial Instruments*

**Affects:** All entities.

**Summary:** The proposed ASU would affect the accounting for a broad range of financial instruments, including investments in debt and equity securities, investments in nonmarketable equity securities, loans, loan commitments, deposit liabilities, trade payables, trade receivables, derivative financial instruments, and debt liabilities. The changes contemplated would affect (1) classification and measurement of financial instruments, (2) accounting for impairment of financial assets, and (3) hedge accounting.

Under the proposed ASU, the default classification and measurement of financial instruments within the scope of the proposed ASU would be fair value, with changes in fair value recognized in net income (FV-NI). However, the proposal does contain exceptions to the default classification and measurement guidance. An entity may elect to recognize and measure certain debt instruments, such as those that meet cash flow and business strategy criteria and that are not hybrid financial instruments, at fair value, with certain unrealized changes in fair value recognized through other comprehensive income (FV-OCI). An entity would also have the option to measure certain financial liabilities at amortized cost if (1) the liability meets the FV-OCI criteria and (2) measuring the financial liability at fair value would create or exacerbate an accounting mismatch. An accounting mismatch may occur, for example, when the financial liability is contractually linked to an asset that is measured at amortized cost. Note that financial liabilities (other than core deposit liabilities) that do not qualify for amortized cost would be classified as FV-NI or FV-OCI (if the conditions discussed above are met). Lastly, on the classification and measurement front, hybrid financial instruments would be recognized and measured at either FV-NI or FV-OCI (if the conditions discussed above are met) and the requirement to bifurcate the embedded feature from the

<sup>3</sup> FASB Accounting Standards Codification Subtopic 205-20, *Presentation of Financial Statements — Discontinued Operations*.

<sup>4</sup> FASB Accounting Standards Codification Subtopic 958-205, *Not-for-Profit Entities — Presentation of Financial Statements*.

host contract would be eliminated. The proposed ASU also would require that once the classification of the financial instrument is determined at initial recognition, it cannot be subsequently changed. This new classification model would result in significant changes to existing GAAP because the current classification categories, such as available for sale and held to maturity, would be eliminated. This classification guidance would also apply to all trade payables and receivables with maturities greater than one year.

In addition, the proposed ASU would require a single approach to accounting for impairment for all financial assets in the FV-OCI category. Unlike current accounting requirements, the proposed ASU would have the same impairment requirements for loans, debt securities, and beneficial interests in securitized financial assets. In determining whether a credit loss exists, an entity would not consider a probability threshold; rather, the entity would consider all past and current events and existing conditions in assessing and calculating the amount of credit impairment. The entity would be required to assess credit impairment in each reporting period and to recognize the credit impairment in earnings. Other unrealized changes in the fair value of the instrument would be recognized in OCI. The proposed impairment model would also prescribe a revised approach for accruing interest income, which would be calculated by applying the effective interest rate to the amortized cost of the financial asset, reduced by any related allowance for credit impairment.

The proposal would also amend the hedge accounting requirements in ASC 815.<sup>5</sup> The changes proposed are consistent with the FASB's 2008 exposure draft<sup>6</sup> on hedge accounting, except that the bifurcation-by-risk approach for financial hedged items in ASC 815 is retained. Some of the proposed ASU's significant changes to hedge accounting would include (1) elimination of the shortcut and critical-terms-match methods; (2) a change in the quantitative assessment of hedge effectiveness criteria from highly effective to reasonably effective; and (3) the inability to dedesignate a hedging relationship simply by removing the hedge designation, unless the criteria for hedge accounting are no longer met or the hedging instrument is sold, is terminated, expires, or is exercised.

**Consideration Points:** Given the comprehensive nature of this project, it would have broad implications for how the underlying information is developed and maintained for financial instruments by other departments within the entity, such as treasury, risk management, and information technology. An entity's risk management and accounting systems may need to be reconfigured to meet the requirements for the (1) increased use of fair value, (2) proposed credit impairment measurement model, (3) proposed interest income recognition model, and (4) proposed hedge accounting model. To comply with the increased fair value requirements, management will need to assess whether it has sufficient internal personnel who are well versed in financial instruments and fair value measurements.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in May 2010; comments on the proposed ASU would be due by September 30, 2010. The FASB staff expects to conduct field visits and roundtables during the third quarter of 2010. The Board expects to begin redeliberating the proposed ASU in the fourth quarter of 2010 and plans to issue a final ASU during the first half of 2011. ●

## Offsetting

**Affects:** All entities.

**Summary:** The FASB recently added a new joint project to its agenda to reconsider the guidance on balance sheet offsetting in ASC 210-20.<sup>7</sup> The Board added this project to its agenda in response to requests from constituents to permit offsetting of securities-lending transactions cleared through a regulated central counterparty. The FASB staff is currently determining the scope of this project. No decisions have been made to date.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the third quarter of 2010. The Board's goal is to issue a final ASU in the first half of 2011. ●

<sup>5</sup> FASB Accounting Standards Codification Topic 815, *Derivatives and Hedging*.

<sup>6</sup> Proposed FASB Statement, *Accounting for Hedging Activities* — an amendment of FASB Statement No. 133. The exposure draft was issued on June 6, 2008.

<sup>7</sup> FASB Accounting Standards Codification Subtopic 210-20, *Balance Sheet: Offsetting*.

## Financial Instruments With Characteristics of Equity

**Affects:** All entities.

**Summary:** Many entities finance their business by issuing hybrid financial instruments that have characteristics of both liabilities and equity. The current accounting requirements governing the classification of financial instruments as liabilities or equity under both IFRSs and U.S. GAAP have been criticized for lacking a clear and consistently applied set of principles and for not distinguishing between equity and nonequity in a manner that best reflects the economics of the transactions involving those instruments. In response to those concerns, the IASB and FASB have agreed to undertake a joint project to improve and simplify the financial reporting for financial instruments with characteristics of equity. In this project, the two boards have developed a new classification approach that would, if finalized, significantly affect the manner in which entities determine whether to classify many financial instruments as liabilities or equity. The project is also expected to provide guidance on how to account for exercises of options and conversions of liabilities into equity instruments. For example, under the new approach:

- Puttable equity instruments (e.g., redeemable equity securities) that are not classified as equity in their entirety would be separated into a liability component and an equity component. Under existing U.S. GAAP, put features embedded in equity securities generally are not accounted for separately from equity host contracts.
- Instruments that require an entity to issue a specified number of its own equity instruments in exchange for a specified price would be classified as equity if certain conditions are met. Under existing U.S. GAAP, no “specified-for-specified” criterion is associated with the assessment of whether contracts for an entity’s own equity should be classified in equity. Currently, ASC 815-40-15<sup>8</sup> permits equity-classified contracts to embody adjustments to the exercise price if the only variables that could affect the settlement would be inputs to the fair value of a fixed-for-fixed forward or option on equity shares.
- Debt instruments that are convertible, at the holder’s option, into a specified number of instruments that will be classified as equity in their entirety upon issuance would be separated into a liability component and an equity component. Other convertible debt instruments would be classified as liabilities in their entirety.

**Consideration Points:** As a result of the proposed changes, an entity would need to assess the impact of the new approach on its debt and equity levels, financial leverage ratios (e.g., debt, debt-to-equity, and interest coverage ratios), return on equity and other financial ratios, earnings, and compliance with debt covenants. In addition, the regulatory capital levels of entities in the financial services industry may be affected.

**Next Steps:** The FASB initially planned to expose the new classification model for comment by the end of June 2010 for a 120-day comment period. The Board had hoped to issue a final ASU during the first half of 2011. However, at its May 11 meeting, the FASB discussed comments it had received on an informal draft of its proposed Accounting Standards Update *Financial Instruments With Characteristics of Equity*. The FASB agreed that further analysis of the comments is warranted and is expected to discuss and agree on next steps jointly with the IASB. In light of the FASB’s discussion, the issuance of an exposure draft on this topic by the end of June 2010, as previously planned, is becoming increasingly unlikely. ●

## Leases

**Affects:** All entities.

**Summary:** For a few years now, the boards have been working on revising the lease accounting model to effectively rid financial reporting of the operating lease classification and their off-balance-sheet treatment. The proposed lease model would focus on an entity’s right to use an asset. Lessees would record a right-of-use asset and a corresponding obligation to pay rentals. Under the performance obligation model for lessors, the leased asset would remain on the lessor’s balance sheet. The lessor would also recognize a receivable for the right to receive rental payments and a corresponding liability representing its obligation to permit the lessee to use the leased asset over the lease term. Note that the boards are reconsidering this performance obligation model along with a derecognition model in which the lessor would partially derecognize the leased asset.

<sup>8</sup> FASB Accounting Standards Codification Subtopic 815-40, *Derivatives and Hedging — Contracts in Entity’s Own Equity*.

The lease term (for both lessees and lessors) would be defined as the longest possible lease term that is more likely than not to occur, which may be longer than the lease term under current U.S. GAAP (e.g., may include additional lease renewal options). In addition, the measurement of lease payments would include expected payments for contingent rentals and residual value guarantees, which would represent a significant change from the current lease accounting model.

The scope of the proposed standard would be generally consistent with current U.S. GAAP; however, contracts that represent the purchase (lessee) or sale (lessor) of the underlying asset would be excluded from the new guidance. The new guidance would indicate that a contract is a purchase or sale if, at the end of the contract, the contract transfers (1) control of the underlying asset and (2) all but a trivial amount of the risks and benefits associated with the underlying asset. In addition, the proposed standard would allow for a simplified form of lease accounting for leases with a maximum possible term of less than 12 months.

The new guidance would also affect the accounting for sale and leaseback transactions. Under the proposed model, these transactions would be accounted for as a sale and leaseback (rather than as a financing) if it is determined that the underlying asset has been sold (see discussion above).

The proposed transition provisions do not contain a grandfathering clause for outstanding leases. A lessee would apply the proposed requirements for leases by recognizing and measuring an obligation to pay rentals and a right-of-use asset for all outstanding leases as of the date of initial application. For simple leases (leases that do not have options, contingent rentals, or residual value guarantees) that are currently classified by lessees as capital leases, the measurement of the assets and liabilities most likely would not be changed on transition or subsequently.

**Consideration Points:** Management should be mindful of the fact that the elimination of operating leases would affect financial ratios and metrics such as debt-to-equity, debt-to-EBITDA,<sup>9</sup> interest coverage, and tangible net worth. For lessees, the new model could also affect certain debt covenants and EBITDA would generally increase as a result of the elimination of rent expense (replaced by amortization and interest expense). The treasury departments of lessee entities would need to consider these factors in their "lease vs. buy" analysis and when negotiating debt covenants. Moreover, the sales forces of lessor entities would need to be cognizant of how the potential accounting affects their clients. The bottom line is that both lessee and lessor entities would need to have a handle on their lease portfolios before these changes take effect.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. However, the boards' reconsideration of the lessors' accounting may delay this timetable. The FASB staff expects to conduct roundtables during the third quarter of 2010. The Board expects to begin redeliberating the proposed ASU in the fourth quarter of 2010 and plans to issue a final ASU during the first half of 2011. ●

## Revenue Recognition

**Affects:** All entities.

**Summary:** This project represents a broad reconsideration of the manner in which an entity recognizes and reports information about revenue resulting from contracts with customers. It would supersede most of the current guidance on revenue recognition in U.S. GAAP, with certain exceptions, doing away with the volumes of industry-specific guidance that many have been using for years. In its place, entities would apply a broad principle when recognizing revenue for contracts under which goods or services are provided to customers. That broad principle would require an entity to (1) identify the contract with a customer, (2) identify the distinct performance obligations, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations, and (5) recognize revenue when the performance obligations are satisfied.

**Consideration Points:** As a result of this project, entities may need to (1) assess their information technology systems, specifically those related to sales, and whether those systems need to be reconfigured; (2) evaluate the existing terms of their contracts and determine how they may affect revenue recognition; (3) educate their sales force on the key aspects of recognizing revenue; and (4) reconsider the timing or the manner in which the sales force is compensated as a result of the changes, if any, in the manner in which revenue is recognized. In addition, because the application of the principles in the proposed standard would most likely require significant judgment, entities may also need to evaluate their accounting policies to ensure consistent

<sup>9</sup> Earnings before interest, taxes, depreciation, and amortization.

application of the principles throughout the entity. Lastly, certain entities may experience significant changes in the amount and timing of revenue recognition and may need to evaluate how and when to disclose such changes to external financial statement users.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. The FASB staff expects to conduct field visits and roundtables during the third quarter of 2010. The Board expects to begin redeliberating the proposed ASU in the fourth quarter of 2010 and plans to issue a final ASU during the first half of 2011. ●

## Consolidations

**Affects:** All entities.

**Summary:** While the FASB recently revised its requirements for consolidation of a variable interest entity, this joint project is a broader reconsideration of the consolidation model as part of an attempt to develop a single, converged model. The proposed model's overall principles are similar to those recently developed by the FASB in ASU 2009-17.<sup>10</sup> However, the scope of this project focuses on all entities, while the FASB's recent revisions focused on structured entities. Some of the expected revisions to the model could change the consolidation result for certain investment managers. Accordingly, entities will need to once again consider whether other entities that they are involved with need to be consolidated.

Like the FASB's recent revisions, the proposed model would focus on which party has the power to direct the activities of the entity that most significantly affect the entity's returns. Evaluating the "power to direct" is not always as straightforward as determining which entity holds a majority of the voting rights. Under the proposed model, holding less than 50 percent of the voting rights also could result in consolidation when other factors indicate that the reporting entity has the power to direct the activities that most significantly affect the entity's returns (e.g., if the reporting entity holds significantly more voting rights than any other party, the other voting rights are widely dispersed, and the reporting entity has the ability to initiate, approve, or veto significant transactions of the entity).

In performing the consolidation analysis, a reporting entity should consider options and convertible instruments; however, these potential voting rights would not be determinative in and of themselves; an entity should consider all facts and circumstances. Further, when assessing whether a decision maker is a principal or an agent, a reporting entity should consider such factors as the scope of decision-making authority, rights held by other parties (including kickout rights), remunerations of the decision maker, and the decision maker's exposure to variability of returns. On balance, this guidance — compared with that in ASU 2009-17 — will most likely result in the identification of more decision makers as agents (particularly investment managers).

Finally, in a manner consistent with current U.S. GAAP, investment companies should measure their investments in entities they control at fair value through profit and loss. The guidance in ASC 946<sup>11</sup> was used as the basis for further developing the attributes of an investment company.

**Consideration Points:** One key challenge is to identify which activities significantly affect the returns of the entity and which party directs these activities. There are often nuances in how entities are structured, and performing this analysis can require the involvement of the entity's various business units and legal departments. Entities would also need to consider whether their existing information technology systems and internal controls are designed to integrate the additional financial reporting information that may be required or whether they would have to develop new systems or data platforms to handle the consolidation and disclosure requirements.

**Next Steps:** The FASB and IASB continue to deliberate the proposed model's disclosure requirements, including the overall disclosure principle, as well as disclosures for subsidiaries, investment companies, and unconsolidated structured entities. The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. The FASB staff expects to conduct roundtables during the third quarter of 2010. The Board expects to begin redeliberating the proposed ASU in the fourth quarter of 2010 and plans to issue a final ASU during the first half of 2011. ●

<sup>10</sup> FASB Accounting Standards Update No. 2009-17, *Improvements to Financial Reporting by Enterprises Involved With Variable Interest Entities*.

<sup>11</sup> FASB Accounting Standards Codification Topic 946, *Financial Services — Investment Companies*.

## Fair Value Measurements

**Affects:** All entities.

**Summary:** This joint project is an attempt to develop a single, converged fair value framework. The proposed changes include the following:

- Amending the highest-and-best-use and valuation premise guidance by clarifying that these concepts are only applicable to measuring the fair value of nonfinancial assets, not financial assets and liabilities.
- Clarifying the fair value measurement of financial assets and liabilities that have offsetting market risks or counterparty credit risks that are managed on a portfolio basis.
- Clarifying the fair value measurement framework related to nonfinancial assets compared with that related to financial assets and liabilities.
- Clarifying that the objective of measuring an individual asset at fair value is to determine the price for a sale of that asset alone, not for a sale of that asset as part of (1) a group of assets or (2) a business. When the highest and best use of an asset is part of a group of assets, an entity can assume that the sale of that asset is to a market participant that has, or can obtain, the complementary assets and complementary liabilities.
- Prohibiting the application of a blockage factor at any level of the fair value hierarchy, since blockage factors were deemed specific to the transaction and not the instrument.
- Requiring sensitivity analysis disclosures for all Level 3 fair value measurements, unless another standard besides ASC 820<sup>12</sup> exempts such a disclosure. The sensitivity analysis disclosures should take into account the effect of the correlation between inputs when relevant.

While there have been no proposed amendments to the scope of ASC 820, entities affected by the projects on accounting for financial instruments and financial instruments with characteristics of equity may experience an increase in the volume of financial assets and liabilities that must be measured at fair value. That is, the proposed amendments to other Codification topics may result in the measurement of more financial assets and liabilities at fair value as opposed to another measurement basis.

**Consideration Points:** For entities that do not currently provide the sensitivity analysis or have it readily available, preparing the proposed disclosures may prove challenging. Entities may need to consider (1) upgrading their information technology systems and existing valuation models to comply with the proposed disclosure requirements and (2) the effect of those disclosure requirements on their internal controls over the financial reporting process. For financial instruments that an entity may be required to measure at fair value as a result of the proposed amendments to other Codification topics, the entity would need to assess whether it has sufficient internal personnel who are well versed in fair value measurements to comply with the increased fair value requirements.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. The comment period would be for a minimum of 45 days, with comments due by August 16, 2010. The FASB staff expects to conduct roundtables during the third quarter of 2010. After the proposed ASU's comment period closes, the boards will jointly redeliberate the comments received. The FASB's goal is to issue a final ASU during the fourth quarter of 2010. ●

## FASB-Only Projects

### Disclosure of Certain Loss Contingencies

**Affects:** All entities.

**Summary:** The FASB plans to expand the scope of loss contingencies that must be disclosed and increase the amount of information that an entity is required to include in those disclosures. In June 2008, the FASB issued an exposure draft<sup>13</sup> on disclosures about certain loss contingencies. The project was undertaken to address financial statement users' concerns that Statement 5<sup>14</sup> (codified in ASC 450-20<sup>15</sup>) does not provide sufficient information on a timely basis about certain remote contingencies or loss contingencies

<sup>12</sup> FASB Accounting Standards Codification Topic 820, *Fair Value Measurements and Disclosures*.

<sup>13</sup> FASB Proposed Statement, *Disclosures About Certain Loss Contingencies*.

<sup>14</sup> FASB Statement No. 5, *Accounting for Contingencies*.

<sup>15</sup> FASB Accounting Standards Codification Subtopic 450-20, *Contingencies — Loss Contingencies*.

in which the loss amount cannot be reasonably estimated. The initial exposure draft would have significantly expanded these requirements by mandating disclosures about certain remote contingencies and, for any contingency (including certain remote contingencies), the claim or assessment amount (or the entity's best estimate of its maximum exposure to loss if there was no claim or assessment amount). Constituents expressed numerous concerns about the proposed guidance, including preparers' difficulties in reliably estimating their exposure to loss, legal concerns about the prejudicial nature of the required disclosures, and auditors' concerns about the reasonable level of assurance that could be obtained regarding some of the proposed disclosures.

Through redeliberations, the FASB has tentatively concluded that (1) entities should provide more robust contingency disclosures as the likelihood and magnitude of a loss increase and as the contingency nears resolution and (2) disclosures about similar contingencies may be aggregated so that they are more understandable and not too detailed. The proposed amendments would not change the recognition and disclosure requirements for loss contingencies that are probable or reasonably possible. However, certain remote contingencies that, because of their nature, potential timing, or potential magnitude, would inform users about the "entity's vulnerability to a potential severe impact" ("special remote") would be subject to disclosure. An entity must use significant judgment when determining whether a remote contingency should be disclosed.

For all loss contingencies that meet the threshold for disclosure (i.e., probable, reasonably possible, or special remote), an entity would disclose (1) publicly available quantitative information; (2) other nonprivileged information that would help users understand and assess the potential loss; and (3) information about potential recoveries from insurance and other sources, but only if (a) such information has been provided to the plaintiff in a litigation contingency or is discoverable or (b) a receivable has been recognized. In addition, if a loss contingency is probable or reasonably possible, an entity would disclose an estimate of the possible loss or range of loss and the amount accrued (if any), unless an estimate cannot be made, in which case the entity should state this fact. Public entities would also be required to include a tabular reconciliation of recognized loss contingencies. The tabular reconciliation should be presented separately for each class of contingencies so that dissimilar contingencies are not aggregated.

In addition to the quantitative disclosures, additional qualitative disclosures would be required for a loss contingency that meets the threshold for disclosure. The proposed guidance would not include an exemption from disclosing prejudicial information ("prejudicial exemption"), since the Board believes it has eliminated many of the speculative/predictive disclosures within the original exposure draft.

**Consideration Points:** As a result of the expanded disclosure requirements, entities would need to evaluate the information technology systems or other processes they use to gather financial statement information. For example, because many of the contingencies that the proposed model would require an entity to disclose may be legal contingencies, the entity would need to maintain a constant dialogue with its legal counsel to gather the information needed for the planned disclosures. In addition, the entity would need to assess the level of aggregation (e.g., product liabilities) in sufficient detail.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. The Board's goal is to issue a final ASU in the third quarter of 2010. ●

## Going Concern

**Affects:** All entities.

**Summary:** This proposed ASU would address (1) management's responsibility to evaluate a reporting entity's ability to meet its obligations for the foreseeable future and (2) the application of the liquidation basis of accounting.

The proposal would require disclosures when management, applying commercially reasonable business judgment, is aware of conditions and events indicating that it is reasonably foreseeable that an entity may not be able to meet its obligations as they become due without making substantial changes to its operating or capital structure. These changes could include, but would not be limited to, a substantial disposition of assets outside the ordinary course of business, restructuring of debt, issuance of equity, or externally or internally forced revisions of its operations. The proposed ASU would require that management take into account available information about the foreseeable future, which is generally, but not limited to, 12 months from the end of the reporting period.

The proposed ASU would require an entity to use the liquidation basis of accounting to prepare its financial statements when liquidation appears imminent. Liquidation is imminent if (1) a plan of liquidation has been approved or (2) the plan to liquidate is being imposed by other forces and it is remote that the entity will continue in operation. Under the proposed ASU, an entity would be required to measure financial statement items to reflect the amount of cash it expects to collect or pay during the course of liquidation.

**Next Steps:** The FASB expects to issue an exposure draft of a proposed ASU in the second quarter of 2010. The Board's goal is to issue a final ASU in the third quarter of 2010. ●

## Key Takeaways

So what should management and others in the financial reporting community think about now as this tidal wave of accounting and financial reporting changes crests? Management should ensure that plans are in place to address each of these projects that are under way at the FASB. Having thoughtful and regular discussions with the affected parties regarding the impact of each of these projects will help ease the transition, turning the tidal wave into a manageable swell in the water. To get those discussions going, we have included a list of questions for entities to consider:

1. Are all necessary groups engaged in the discussions regarding these changes?
2. What are the key differences between current accounting policies and proposed changes to U.S. GAAP? How will these accounting changes affect critical accounting policies and management's estimates?
3. How will the proposed changes affect the financial statements, capital ratios, debt covenants, and internal controls over financial reporting?
4. Are sufficient and knowledgeable resources available to address these accounting changes?
5. Are information technology systems able to integrate the proposed changes?
6. Will these accounting changes require the increased use of external specialists?
7. What educational needs and goals do the board and audit committee have? How will the changes affect the financial expert designation?
8. How will the changes affect the duties and responsibilities of the audit committee with respect to internal control and financial statement disclosure?
9. What information, if any, will need to be communicated to external financial statement users?

Still uneasy about the significance of these changes? Stay tuned for further communications regarding each of these projects (e.g., *Heads Up* articles and *Dbriefs* webcasts). In addition, feel free to reach out to a Deloitte representative to have more detailed discussions regarding these projects, the accounting changes they represent, or the business impact they may pose.

## Subscriptions

If you wish to receive *Accounting Roundup* and other accounting publications issued by Deloitte's Accounting Standards and Communications Group, please [register](#) at [www.deloitte.com/us/subscriptions](http://www.deloitte.com/us/subscriptions).

## Technical Library: The Deloitte Accounting Research Tool

Deloitte makes available, on a subscription basis, access to its online library of accounting and financial disclosure literature. Called Technical Library: The Deloitte Accounting Research Tool, the library includes material from the FASB, the EITF, the AICPA, the PCAOB, the IASB, and the SEC, in addition to Deloitte's own accounting and SEC manuals and other interpretive accounting and SEC guidance.

Updated every business day, Technical Library has an intuitive design and navigation system that, together with its powerful search features, enable users to quickly locate information anytime, from any computer. In addition, Technical Library subscribers receive *Technically Speaking*, the weekly publication that highlights recent additions to the library.

For more information, including subscription details and an online demonstration, visit [www.deloitte.com/us/techlibrary](http://www.deloitte.com/us/techlibrary).

Conclusions of the FASB, GASB, IASB, and IFRIC are subject to change at future meetings and generally do not affect current accounting requirements until an official position (e.g., Accounting Standards Update or IFRS) is issued. Official positions are determined only after extensive deliberation and due process, including a formal vote.

Further information about the standard setters can be found on their respective Web sites as follows: [www.fasb.org](http://www.fasb.org) (FASB); [www.fasb.org/eitf/agenda.shtml](http://www.fasb.org/eitf/agenda.shtml) (EITF); [www.aicpa.org](http://www.aicpa.org) (AICPA); [www.sec.gov](http://www.sec.gov) (SEC); [www.fasab.gov](http://www.fasab.gov) (FASAB); [www.gasb.org](http://www.gasb.org) (GASB); and [www.iasb.org](http://www.iasb.org) — or on [www.iasplus.com/index.htm](http://www.iasplus.com/index.htm) (IASB and IFRIC).

*Accounting Roundup* is prepared by the National Office Accounting Standards and Communications Group of Deloitte. 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.

This publication contains general information only and Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. Deloitte, its affiliates, and related entities shall not be responsible for any loss sustained by any person who relies on this publication.

As used in this document, "Deloitte" means Deloitte & Touche LLP, a subsidiary of Deloitte LLP. Please see [www.deloitte.com/us/about](http://www.deloitte.com/us/about) for a detailed description of the legal structure of Deloitte LLP and its subsidiaries.