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Although this summary of the discussions and views expressed is believed to be accurate, no representations can be made that it is complete or without error. Official meeting highlights are prepared by the American Institute of Certified Public Accountants (AICPA) and approved by the Securities and Exchange Commission (SEC) and sometimes contain additional information, updates on issues discussed, and, in some instances, revisions to the views expressed at the meeting; therefore, this meeting summary is not a substitute for the official AICPA highlights. Views expressed at the joint meeting are not authoritative positions or interpretations and do not represent an official position of the AICPA, SEC, or Financial Accounting Standards Board (FASB) and are subject to change.

AICPA SEC Regulations Committee and SEC Staff Hold Third Meeting of 2006 (Revised February 14, 2007*)

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

Update: Since the original issuance of this *Heads Up*, certain of the final discussion documents related to the September 26, 2006, meeting were posted to the AICPA's Web site. These documents contain the final views of the SEC staff on certain issues discussed at the meeting.

We have revised the "SEC Staff Views" within the Appendix for issues on which the final discussion documents differ substantively from the original issuance of this *Heads Up*. Those issues are denoted (revised or further revised), and there is a brief summary of the reason for the revision after the SEC view.

At this time, not all of the final discussion documents have been posted to the AICPA's Web site. This meeting summary is not a substitute for the official AICPA highlights. Readers of this document should check the AICPA's Web site for the final discussion documents once they are issued.

On September 26, 2006, the AICPA SEC Regulations Committee ("Regulations Committee") held its third meeting of the year with the SEC staff. The Regulations Committee is composed of representatives from public accounting firms, industry, and academia, and meets periodically with the SEC staff to discuss emerging technical accounting and reporting issues relating to SEC rules and regulations.

At this meeting, in addition to discussing the agenda items relating to technical accounting and reporting issues, the SEC staff discussed ongoing projects, final rule releases, and other matters.

SEC Staff Discussions Regarding Ongoing Projects, Final Rule Releases, and Other Matters

Staff Accounting Bulletin 108

The Office of the Chief Accountant recently issued SEC Staff Accounting Bulletin (SAB) 108,[1] regarding the process of quantifying financial statement misstatements.

* The issues in the Appendix, "Disclosures Under Interpretation 48 in Form 10-Q in the Period of Adoption" and "Income Statement Classification of Interest and Penalties for Income Tax Deficiencies Under Interpretation 48," have been further revised as of this date.

[1] 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."

The SEC staff is considering developing guidance about quantifying financial statement misstatements on a quarterly basis, for the following reasons:

1. The relevant recommendations of the SEC Advisory Committee on Smaller Public Companies ("Advisory Committee") (see the report on the SEC's Web site).
2. The provisions of paragraph 29 of APB Opinion No. 28, *Interim Financial Reporting*, which states that when "determining materiality for the purpose of reporting the cumulative effect of an accounting change or correction of an error, amounts should be related to the estimated income for the full fiscal year and also to the effect on the trend of earnings. Changes that are material with respect to an interim period but not material with respect to the estimated income for the full fiscal year or to the trend of earnings, should be separately disclosed in the interim period." [Footnote omitted]

The SEC staff has not yet determined what form the guidance will take.

Editor's Note: For example, one of the Advisory Committee's recommendations in its final report was that the SEC consider issuing guidance for all public companies on materiality related to previously issued financial statements. The Advisory Committee report also points out that SEC Staff Accounting Bulletin No. 99, *Materiality*, does not address the assessment of materiality in quarterly reporting periods, including quarterly reporting periods of previously reported annual periods.

SAB 108 states, "Correcting prior year financial statements for immaterial errors would not require previously filed reports to be amended. Such correction may be made the next time the registrant files the prior year financial statements." The SEC staff confirmed that, in cases where a pending restatement is immaterial, a registrant would not be required to file a Form 8-K[2] to notify investors that previously issued financial statements could no longer be relied upon, although the filing of this current report is a matter of judgment. However, the SEC staff cautioned that, if the error being corrected materially affected a prior quarter of the current fiscal year, the SEC staff would expect the registrant to file such a Form 8-K with respect to those interim financial statements.

The SEC staff indicated that it plans to discuss SAB 108 at the 2006 AICPA National Conference on Current SEC and PCAOB Developments in December. SAB 108 can be obtained from the SEC's Web site. Readers can also refer to Deloitte & Touche's *Heads Up* and SEC Alert on the SAB.

Office of the Chief Accountant Letter on Application of Stock Option Literature

Chief Accountant Conrad Hewitt recently issued a letter expressing the SEC staff's views on the appropriate application of existing accounting guidance related to stock option grants. During the Regulations Committee meeting, the SEC staff emphasized that the letter does not address manipulative backdating of stock options. The SEC staff also indicated that it has not provided further formal guidance or information on this issue since the letter was released and is not aware of any additional information that should have been included in the letter.

The Regulations Committee asked the SEC staff to clarify the following statement in the letter: "The staff understands that errors related to the issues addressed in this letter may affect several years of filings, and that companies may believe that amending all of the affected filings is unnecessary. Companies that propose to correct material errors without amending all previously filed reports should contact the staff of the Division of Corporation Finance." However, the SEC staff provided no further guidance at the meeting. The SEC staff did indicate that it may issue general guidance and additional factors registrants should consider in evaluating filings that require amendment relating to the dating of stock options, and added that the guidance may be in the form of a Division of Corporation Finance chief accountant's alert or a letter to CFOs.

The Regulations Committee indicated that there may be practical issues related to filing amendments for periods audited by a predecessor auditor. The SEC staff emphasized that a registrant should not conclude that a restatement is not required just because the error is immaterial in the current period when a large adjustment occurred several years ago. A registrant needs to evaluate all periods affected by the error.

The SEC staff expects transparent disclosure, including an analysis in the notes to the financial statements of the amount of the cumulative restatement of beginning retained earnings along with a schedule showing the amount attributable to each previous fiscal year, when any filing relief related to previous filings is provided.

[2] Item 4.02(a) of Form 8-K.

The letter can be accessed at the SEC's Web site. Readers can also refer to Deloitte & Touche's *Heads Up* on the letter.

Recent GAO Report on Restatements

A recent Government Accountability Office (GAO) report on restatements observed that many registrants are not filing a Form 8-K[3] to notify investors that previously issued financial statements cannot be relied upon when registrants conclude that their historical financial statements need to be restated for the correction of an error. Some registrants are simply disclosing this information within a Form 10-Q or Form 10-K filing. The GAO recommended that the SEC clarify and harmonize its rules so that the Form 8-K requirement is better understood. The GAO report can be obtained at the GAO's Web site.

The SEC staff indicated that its position regarding the filing of Form 8-K has not changed, and the determination by a registrant to file is one that requires judgment by the registrant. The SEC staff indicated that it is investigating instances in which registrants should have filed Form 8-K but failed to do so.

Review of Registrant Filings

The SEC staff is still reviewing 2005 Form 10-K filings with the expectation of meeting deadlines required by the Sarbanes-Oxley Act of 2002 for review of all public companies at least once every three years. The SEC staff initially focused its reviews on larger companies, but has started reviews of some smaller companies and expects to issue any comment letters before the end of the year.

In large part, the issues raising comments are similar to those noted in previous reporting seasons and include the following issues:

- Classification errors in the statement of cash flows, including the determination of materiality of the error.
- Fair value issues, including the determination and reasonableness of the methodology and assumptions used.
- Critical accounting estimates, including the appropriateness of disclosures related to factors affecting the estimates.
- Non-GAAP measures, including the exclusion of recurring charges.
- Hedge accounting, primarily related to the financial services industry.
- Disclosures required by EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock," including accounting and disclosure for convertible instruments and warrants.
- Documentation of policy elections under EITF Issue No. 05-4, "The Effect of a Liquidated Damages Clause on a Freestanding Financial Instrument Subject to Issue No. 00-19."
- Determination and aggregation of operating segments under FASB Statement No. 131, *Disclosures About Segments of an Enterprise and Related Information*.
- Proper revenue recognition based on the terms and conditions of sales agreements.

Other Items

- An update of the Division of Corporation Finance Accounting Disclosure Rules and Practices Training Manual is still in progress. An expected completion date has not been set.
- An update of the Current Accounting and Disclosures Issues in the Division of Corporation Finance is in process, and the SEC staff anticipates issuing the update in 2006. The staff indicated there are not expected to be any new significant items included in the update.

[3] Item 4.02(a) of Form 8-K.

Summary of SEC Staff Views on Issues Discussed With Regulations Committee

The following is a brief description of each issue that was part of the agenda discussed at the September 26, 2006, meeting. The attached Appendix contains more background information and details of the views expressed. (Readers may click any title to be taken to a detailed description in the Appendix.)

Title	Scope and Description
Section 404 Reporting by Non-Accelerated Filers After Exiting Accelerated Filing Status	**Scope:** Applicable to registrants who reported as accelerated filers or large accelerated filers in the prior year but become non-accelerated filers in the current year. **Description:** This issue addresses whether a registrant who was an accelerated filer or large accelerated filer in the prior year, but becomes a non-accelerated filer in the current year, must comply with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 in its current-year SEC annual report.
Determining Whether Financial Statements of a Significant Equity Method Investee Are Required in the Year in Which an Investee Is Disposed **(revised)**	**Scope:** Applicable to registrants that have disposed of an equity method investee. **Description:** This issue focuses on whether a registrant is required to provide financial statements of a significant equity method investee in the year in which the registrant disposes of its investment.
Treatment, in Pre-Adoption Pro Forma Income Statement, of Options Given to Employees of a Target in a Business Combination After the Acquirer Has Adopted Statement 123(R)	**Scope:** Applicable to registrants that acquire a business after adopting FASB Statement No. 123(R), *Share-Based Payment*, and grant replacement stock options to the employees of the acquired company. **Description:** This issue addresses how compensation expense related to replacement stock options granted as part of an acquisition should be treated in the registrant's pro forma income statement of the year prior to the adoption of Statement 123(R), and whether such treatment depends on the transition method used by the registrant.
Labeling Financial Statement Columns to Indicate a Change in Accounting Principle	**Scope:** Applicable to registrants that have adjusted prior-year financial statements to reflect retrospective application of a new accounting principle. **Description:** This issue addresses whether registrants that have adjusted prior-year financial statements included in a current year filing as a result of the retrospective application of a new accounting principle, as required by FASB Statement No. 154, *Accounting Changes and Error Corrections*, should label such financial statements "As Adjusted."
Disclosures Under Interpretation 48 in Form 10-Q in the Period of Adoption **(further revised)**	**Scope:** Applicable to registrants that have adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*. **Description:** This issue addresses the disclosure requirements for registrants in the first interim period in which Interpretation 48 is adopted and subsequent interim periods until disclosures are included in the registrant's annual Form 10-K filing.
Income Statement Classification of Interest and Penalties for Income Tax Deficiencies Under Interpretation 48 **(further revised)**	**Scope:** Applicable to registrants that have adopted Interpretation 48. **Description:** This issue addresses whether a registrant needs to obtain a preferability letter if it changes its income statement classification of interest and/or penalties related to income tax deficiencies in connection with or after the adoption of Interpretation 48.

Appendix: Background Information and Details on Views Expressed

Section 404 Reporting by Non-Accelerated Filers After Exiting Accelerated Filer Status

In December 2005, the SEC issued a final rule, *Revisions to Accelerated Filer Definition and Accelerated Deadlines for Filing Periodic Reports*,[4] which amended the provisions for exiting accelerated filer status. The new rule states that an accelerated filer,[5] or a large accelerated filer,[6] whose public float[7] falls below $50 million as of the last business day of its second fiscal quarter would exit accelerated filer status at the end of the fiscal year and would file its annual report for that year and it would file subsequent periodic reports on a non-accelerated basis (i.e., file its Form 10-K within 90 days after year end and its Form 10-Qs within 45 days after quarter end). Also, an accelerated filer or large accelerated filer that ceases to have any public float (e.g., an entity that is acquired and continues to be a filer as a result of having outstanding public debt) would immediately become a non-accelerated filer. Under the prior rules, an accelerated filer had to file as such until it qualified to file as a small business issuer.[8]

In addition to these accelerated filer status rule changes, the SEC has adopted various revisions[9] to the transition provisions for certain foreign and domestic registrants to begin to comply with the internal control reporting requirements of Section 404 of the Sarbanes-Oxley Act of 2002 ("Section 404"). In light of these rule changes, and the pending proposal by the SEC to further delay Section 404 reporting requirements for non-accelerated filers and newly public companies,[10] the Regulations Committee asked the SEC staff to confirm that the Section 404 transition provisions apply to all non-accelerated filers, including a former accelerated or large accelerated filer that became a non-accelerated filer. That is, the Regulations Committee sought confirmation that a former accelerated filer or large accelerated filer that had previously reported under Section 404 could suspend its Section 404 reporting requirements while categorized as a non-accelerated filer until it either (a) again becomes an accelerated filer or (b) must begin to comply with Section 404 as a non-accelerated filer under the SEC's applicable transition provisions.

SEC Staff View: The SEC staff confirmed that the Section 404 transition provisions apply to all non-accelerated filers, including a former accelerated or large accelerated filer that has become a non-accelerated filer. The SEC staff further noted that an accelerated filer previously subject to Section 404 reporting should reassess its Section 404 reporting requirements if it becomes a non-accelerated filer.

Editor's Note: Company X is a calendar-year-end SEC registrant. For its fiscal year ended December 31, 2005, Company X was an accelerated filer and complied with all applicable SEC filing and Section 404 reporting requirements and deadlines. For its fiscal year ending December 31, 2006, Company X will qualify as a non-accelerated filer by virtue of its public float dropping below $50 million as of the last business day of its second fiscal quarter (June 30, 2006). As a non-accelerated filer, Company X is not required to comply with Section 404 in its 2006 Form 10-K.

Determining Whether Financial Statements of a Significant Equity Method Investee Are Required in the Year in Which an Investee Is Disposed **(revised)**

This issue is a revisit of discussions with the SEC staff at the Regulations Committee meetings on June 12, 2001, June 14, 2005, and June 20, 2006.

As discussed in Deloitte & Touche's SEC Alert 06-1 on the June 20, 2006, Regulations Committee Meeting, Rule 3-09[11] requires a registrant to provide financial statements of a significant equity method investee. The significance

[4] SEC Release Nos. 33-8644, 34-52989, dated December 21, 2005.

[5] An issuer with aggregate worldwide market value of voting and non-voting common equity held by non-affiliates of the issuer of $75 million or more, but less than $700 million, as of the last business day of the issuer's most recently completed second fiscal quarter.

[6] An issuer with aggregate worldwide market value of voting and non-voting common equity held by non-affiliates of the issuer of $700 million or more, as of the last business day of the issuer's most recently completed second fiscal quarter.

[7] Also referred to as worldwide market value of outstanding voting and non-voting common equity held by non-affiliates.

[8] As defined by SEC Regulation 230.405, a registrant that (1) has revenues of less than $25 million; (2) is a U.S. or Canadian issuer; (3) is not an investment company; and (4) if a majority owned subsidiary, the parent corporation is also a small business issuer.

[9] SEC Release Nos. 33-8618; 34-52492, dated September 22, 2005, for domestic filers and SEC Release Nos. 33-8730A; 34-54294A dated August 9, 2006, for foreign private issuers that are accelerated filers.

[10] SEC Release Nos. 33-8731; 34-54295, dated August 9, 2006.

[11] SEC Regulation S-X, Rule 3-09, "Separate Financial Statements of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons."

tests include an income test that requires a comparison of income from continuing operations before income taxes, extraordinary items, and cumulative effect of a change in accounting principle of the investee with such consolidated income of the registrant and its subsidiaries for the most recently completed fiscal year.[12] In some cases, the inclusion of the gain or loss on disposal of the equity method investee has caused an equity method investee that has not historically been significant to become significant, and thus has required the registrant to include the investees' financial statements in its filing for the first time in the year of disposal. The SEC staff has previously taken the view that Rule 3-09 applies in the year of disposal, and that any gain or loss on disposal must be included in the numerator for the income test required by Rule 3-09 when determining significance.

The Regulations Committee asked the SEC staff to reconsider its previous views in situations where a registrant has disposed of the investment based on the Regulation Committee's view that disclosures required by APB Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*,[13] paragraph (g) of SEC Regulation S-X, Rule 4-08, "General Notes to Financial Statements,"[14] and management's discussion and analysis rules,[15] provide sufficient details to investors. The Regulations Committee also requested that the SEC staff consider recommending amendments to Rule 3-09 to address this issue as well as other related practice issues.

SEC Staff View: The SEC staff noted that its views on these matters have not changed. Rule 3-09 does apply in the year of disposition of the investee, and any gain or loss on disposal must be included in the numerator for the income test required by Rule 3-09 when determining significance.

As noted in the initial *Heads Up*, the SEC staff indicated at the meeting that it would consider recommending amendments to Rule 3-09 to reflect the above view. The preliminary SEC staff view on this issue has been revised because the final discussion document did not include such an indication.

Treatment, in Pre-Adoption Pro Forma Income Statement, of Options Given to Employees of a Target in a Business Combination After the Acquirer Has Adopted Statement 123(R)

This issue is a revisit of a discussion with the SEC staff at the Regulations Committee meeting on June 20, 2006.

As part of acquisitions, registrants often grant their stock options to employees of an acquired company in exchange for previously held stock options in the acquiree company ("replacement" options). In accordance with FASB Statement No. 123(R), *Share-Based Payment*, the expense related to the unvested portion of the replacement stock options in the acquiree company generally is recognized as compensation expense by the registrant.

The Regulations Committee asked the SEC staff how the compensation expense should be treated in the pro forma income statement to be filed on Form 8-K related to the year prior to the registrant's adoption of Statement 123(R) and whether such treatment depends on the registrant's method of adoption — that is, the modified retrospective or the modified prospective transition method.

The following example was provided to the SEC staff at the September 26, 2006, meeting:

> Company X is a calendar year-end SEC registrant with publicly traded equity. Company X has an employee stock option plan that it has historically accounted for under APB Opinion No. 25, *Accounting for Stock Issued to Employees*, with pro forma disclosures in the notes to the financial statements, as required by FASB Statement No. 123, *Accounting for Stock-Based Compensation*, as amended by FASB Statement No. 148, *Accounting for Stock Based Compensation — Transition and Disclosure*.
>
> Company X adopted the provisions of Statement 123(R) effective January 1, 2006, and filed its March 31, 2006, Form 10-Q on May 1, 2006. Company X acquired a significant business in June 2006; accordingly, Company X's Form 8-K must include pro forma income statements for the year ended December 31, 2005, and for the three months ended March 31, 2006.

12 As required by paragraph (w) of SEC Regulation S-X, Rule 1-02, "Definition of Terms Used in Regulation S-X."
13 The Opinion requires detailed disclosures about the equity method investee, such as percentage of ownership in the equity method investee and differences between the carrying value and the difference, if any, between the amount at which an investment is carried and the amount of underlying equity in net assets and the accounting treatment of the difference.
14 The Rule requires summarized financial information of the investee.
15 The rules require detailed discussions of material changes in results from operations, such as those that could be caused by a disposal of a significant equity method investee.

SEC Staff View: In situations in which the acquirer has adopted the **modified retrospective transition method,** the SEC staff believes the pro forma income statements referred to in the example above should include an adjustment to reflect projected compensation expense related to the stock options granted on the acquisition date. The adjustment should be computed in accordance with Statement 123(R) since this was the accounting standard applicable to the stock options issued in connection with the acquisition. In addition, a pro forma adjustment should be made to eliminate the compensation expense, if any, reflected in the acquired company's historical financial statements related to stock options exchanged in the business combination. This will eliminate the potential double counting of compensation expense.

The SEC staff's view is based on the premise that the additional stock options granted in connection with the acquisition essentially represent a change in pay level for the acquired company's employees that was made in connection with the acquisition. Because the amount is supportable and directly attributable to the transaction, an adjustment is required.

The SEC staff noted that the fact that these adjustments are not computed in the same manner as the adjustments retrospectively reflected in the registrant's financial statements is not relevant. Rather, the fact that these adjustments will affect the registrant's financial statements after the acquisition date is relevant.

In situations in which the acquirer has adopted the **modified prospective transition method**, the SEC staff asked for additional time to consider the matter.

Labeling Financial Statement Columns to Indicate a Change in Accounting Principle

In accordance with the adoption of FASB Statement No. 154, *Accounting Changes and Error Correction*s, registrants are required to adjust prior period financial statements to reflect the retrospective application of a new accounting principle. Questions have arisen about whether labeling the prior period column headings in the registrant's financial statements "As Adjusted" is required or simply encouraged. Such guidance is not provided within Statement 154, and the Division of Corporation Finance Accounting and Disclosure Rules and Practices Training Manual only addresses situations in which financial statements have been restated, rather than adjusted.

SEC Staff View: The SEC staff encourages, but does not require, labeling of column headings "As Adjusted" for a change in accounting principle affected by retrospective application. The SEC staff added that while labeling financial statements is not required for the retrospective application of a new accounting principle, it is considered a best practice to facilitate transparency. Registrants should ensure their filings allow a reader to easily understand that changes and/or corrections have occurred.

Disclosures Under Interpretation 48 in Form 10-Q in the Period of Adoption **(further revised)**

The SEC staff has historically required registrants to present all disclosures required by a new accounting standard in the first Form 10-Q when that standard is adopted during an interim period. Further, the SEC staff has required that these disclosures continue to be provided in subsequent Form 10-Qs until the first Form 10-K is filed that contains the required disclosures.

FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, will be effective in the first interim period for fiscal years beginning after December 15, 2006. Paragraphs 20 and 21 of Interpretation 48 present several disclosures that are required annually. However, since Interpretation 48 does not require or permit retrospective application, the Regulations Committee asked the SEC staff to provide guidance on the initial disclosure of information related to annual periods in the interim period of adoption.

SEC Staff View: The SEC staff stated that the required disclosures related to Interpretation 48 as of the date of adoption and as of the interim periods after adoption are as follows:

Interpretation 48 Disclosures	Disclosure as of Date of Adoption[16]	Disclosure as to Interim Periods After Adoption[17]
20. An enterprise shall disclose its policy on classification of interest and penalties, in accordance with paragraph 19 of this Interpretation, in the footnotes to the financial statements.	Yes[19]	Disclose any change in classification
21. An enterprise shall disclose the following at the end of each annual reporting period presented:		
a. A tabular reconciliation of the total amounts of unrecognized tax benefits at the beginning and end of the period, which shall include at a minimum:	Total amount of unrecognized tax benefits as of date of adoption	Tabular reconciliation not required for interim periods
(1) The gross amounts of increases and decreases in unrecognized tax benefits as a result of tax positions taken during a prior period	N/A	Disclose any material changes
(2) The gross amounts of increases and decreases in unrecognized tax benefits as a result of tax positions taken during the current period	N/A	Disclose any material changes[18]
(3) The amounts of decreases in the unrecognized tax benefits relating to settlements with taxing authorities	N/A	Disclose any material changes[18]
(4) Reductions to unrecognized tax benefits as a result of a lapse in the applicable statute of limitations	N/A	Disclose any material changes[18]
b. The total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate	Yes, amount of as of date of adoption	Disclose any material changes

Interpretation 48 Disclosures	Disclosure as of Date of Adoption[16]	Disclosure as to Interim Periods After Adoption[17]
c. The total amounts of interest and penalties recognized in the statement of operations and the total amounts of interest and penalties recognized in the statement of financial position[19]	Total amount of accrued interest and penalties as of date of adoption	Disclose any material changes[19]
d. For positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease within 12 months of the reporting date:	Yes, amount of as of date of adoption	Disclose any material changes[20]
(1) The nature of the uncertainty	Yes, as of date of adoption	Disclose any material changes
(2) The nature of the event that could occur in the next 12 months that would cause the change	Yes, as of date of adoption	Disclose any material changes
(3) An estimate of the range of the reasonably possible change or a statement that an estimate of the range cannot be made	Yes, estimate of as of date of adoption	Disclose any material changes
e. A description of tax years that remain subject to examination by major tax jurisdictions	Yes, as of date of adoption	Disclose any material changes

16 Disclose in all interim financial statements in the year of adoption.

17 Regarding interim balances or activity during the current and year-to-date interim periods.

18 If material amounts are recognized during the quarter, disclosure in management's discussion and analysis may be required.

19 See SEC Staff view below regarding supplemental disclosures for interest and penalties in pre-adoption periods.

20 If material amounts are updated during the quarter disclosure in management's discussion and analysis may be required and critical accounting policies may need to be updated.

In addition, registrants should consider the following disclosures regarding the classification of interest and penalties:

Change in Classification Upon Adoption: If upon adoption of Interpretation 48 a registrant adopts a new financial statement classification of interest and penalties, it should disclose that it has adopted a new accounting principle and disclose its new policy for classification of interest and penalties. Because Interpretation 48 transition does not allow any form of retroactive application, financial statements for periods presented prior to adoption of

Interpretation 48 should not be retroactively restated or reclassified to conform to the newly adopted accounting principle. However, a registrant should disclose its policy for the classification of interest and penalties for prior periods.

Change in Classification Subsequent to Adoption: If subsequent to the first quarter of the year of adoption of Interpretation 48 a registrant changes its financial statement classification of interest and penalties, it should provide the disclosures specified by paragraphs 17 and 18 of Statement 154 and file a preferability letter (post adoption). This change in accounting principle would be retrospectively applied beginning with the first interim period in which Interpretation 48 was applied. Periods prior to the adoption of Interpretation 48 should not be retroactively restated or reclassified because Interpretation 48 transition does not allow retroactive application.

Additional Disclosures for Such Changes in Classification: If a registrant has changed its classification policy, the SEC staff believes the registrant should disclose, in annual financial statements that include any period prior to the adoption of Interpretation 48, both the classification and amount of interest and penalties on uncertain income tax positions reflected in each income statement. In those circumstances, if the registrant cannot determine the amount of interest and penalties for periods prior to the adoption of Interpretation 48 due to its inability to disaggregate the interest or penalties portion of the accrual from the underlying tax exposure, it should disclose that fact.

As noted in the initial *Heads Up*, at the meeting, the SEC staff asked for additional time to consider this issue. The staff's revised view above reflects the disclosures required, as noted in the final discussion document.

Income Statement Classification of Interest and Penalties for Income Tax Deficiencies Under Interpretation 48 **(further revised)**

Paragraph (b)(18) of SEC Regulation S-K Item 601, "Exhibits," requires registrants to demonstrate preferability and to obtain a preferability letter for a change in accounting principle, except when the change results from the adoption of a new accounting standard. The classification of interest and penalties on income tax deficiencies is not addressed in FASB Statement No. 109, *Accounting for Income Taxes*. Interpretation 48 permits, on the basis of the accounting policy election of the enterprise, interest to be classified in the financial statements as either income taxes or interest expenses, and penalties to be classified in the financial statements as either income taxes or another expense classification. An enterprise must consistently apply and disclose its policy on classification. At issue is whether a registrant needs to obtain a preferability letter if it changes its income statement classification of interest and/or penalties on income tax deficiencies either upon or after the adoption of Interpretation 48.

SEC Staff View: With regard to a change in income statement classification of interest or penalties related to income tax deficiencies **upon** the adoption of Interpretation 48, the SEC staff took the view that two possible methods of presentation (either within other income (expense) or within tax provision (benefit)) existed before the adoption of Interpretation 48 and continue to exist after the adoption of Interpretation 48. The SEC staff believes that because the accounting model for tax contingencies and interest has fundamentally changed, registrants are not required to obtain a preferability letter upon adoption of Interpretation 48.

The preliminary SEC staff view on this issue has been revised. As noted in the initial *Heads Up*, the SEC staff indicated at the meeting that a preferability letter would be required if a registrant made a material change to its previous accounting policy or practice regarding the classification of interest and/or penalties on income tax deficiencies upon adoption of Interpretation 48. However, upon further consideration, the SEC staff revised its view, and the final discussion document indicates that neither justification of the change as preferable nor a preferability letter would be required in such circumstances.

With regard to a change in income statement classification of interest or penalties related to income tax deficiencies **after** the adoption of Interpretation 48, the SEC staff believes that a registrant is required to obtain a preferability letter for a material change in the registrant's accounting policy.

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