

# Accounting Roundup

April 26, 2004

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

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## FASB Developments

### **FASB Issues FSP FAS 129-1, *Disclosure Requirements Under FASB Statement No. 129, Disclosure of Information About Capital Structure, Relating to Contingently Convertible Securities***

On April 9, 2004, the FASB issued FSP FAS 129-1 to provide disclosure guidance for contingently convertible securities, including those instruments with contingent conversion requirements that have not been met and otherwise are not required to be included in the computation of diluted earnings per share. The FSP addresses concerns that disclosures relating to contingently convertible securities are inconsistent between companies or may be inadequate. FSP FAS 129-1 notes that to comply with the requirements of SFAS 129, the significant terms of the conversion features of the contingently convertible security should be disclosed to enable users of financial statements to understand the circumstances of the contingency and the potential impact of conversion. Companies' disclosures should include:

- Events or changes in circumstances that would cause the contingency to be met and any significant features necessary to understand the conversion rights and the timing of those rights (e.g., the periods in which (1) the contingency might be met and (2) the securities may be converted if the contingency is met)
- The conversion price and the number of shares into which the security is potentially convertible
- Events or changes in circumstances, if any, that could adjust or change the contingency, conversion price, or number of shares, including significant terms of those changes
- The manner of settlement upon conversion and any alternative settlement methods (e.g., cash, shares, or a combination).

The FSP further states that the disclosures should indicate whether the shares that would be issued, if the contingently convertible securities were converted, are included in the calculation of diluted earnings per share, and the reasons why or why not.

Disclosure of the impact of derivative transactions entered into in connection with the issuance of the contingently convertible securities should be provided, if they are necessary

to help fully explain the potential impact of the contingently convertible securities.

The FSP is effective immediately and applies to all existing and newly created securities.

FSP FAS 129-1 is available on the FASB's Web site.

## **FASB Issues Proposed FSPs**

### **Proposed FSPs FAS 141-a and FAS 142-a, *Interaction of FASB Statements No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets, and EITF Issue No. 04-2, Whether Mineral Rights are Tangible or Intangible Assets***

On April 2, 2004, the FASB issued proposed FSPs FAS 141-a and FAS 142-a to address inconsistencies between the consensus reached for EITF 04-2 and guidance provided in SFAS 141 and SFAS 142 regarding whether mineral rights are tangible or intangible assets. The proposed FSPs amend SFAS 141 and 142 to conform them to the EITF consensus that certain mineral rights are tangible assets.

The FSPs will be effective for the first reporting period beginning after the date that the FSPs are finalized. If adopting the FSP results in recharacterization of an asset, prior period amounts in the statements of financial position should be reclassified, and any effects on amortization or depreciation of the asset should be accounted for prospectively.

FSPs FAS 141-a and FAS 142-a are available on the FASB's Web site. The comment period ended April 16, 2004.

### **Proposed FSP FAS 97-a, *Situations in Which Paragraphs 17(b) and 20 of FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses From the Sale of Investments, Permit or Require Accrual of an Unearned Revenue Liability***

On April 2, 2004, the FASB issued proposed FSP FAS 97-a to address inconsistencies that exist in practice regarding when it is appropriate to recognize an unearned revenue liability under SFAS 97. This disparity in practice became evident when companies adopted SOP No. 03-1, *Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts*.

SFAS 97 specifies the components of the liability for policy benefits for universal life-type contracts, and states that the liability should include "any amounts that have been assessed [against the contract holder's account balance] to compensate the insurer for services to be performed over future periods." SOP 03-1 requires such a liability to be recorded "if the amounts assessed against the contract holder each period for the insurance benefit feature are assessed in a manner that is expected to result in profits in earlier years and losses in

subsequent years from the insurance benefit function."

Proposed FSP FAS 97-a clarifies whether it is appropriate to recognize an unearned revenue liability to compensate the insurer for services to be performed over future periods when future profits are expected to decline from the current level, or only when current profits are expected to be followed by future losses (consistent with SOP 03-1). The FSP states that the guidance in SOP 03-1 addresses only one situation, and does not limit the SFAS 97 requirement to recognize a liability for unearned revenue only to those situations in which profits are expected to be followed by losses.

FSP FAS 97-a is available on the FASB's Web site. The comment period ends May 3, 2004.

## **FASB Does Not Clear AcSEC's Proposed SOP on Property, Plant, and Equipment**

On April 14, 2004, the FASB voted unanimously not to clear AcSEC's draft SOP on property, plant, and equipment. The Board anticipates considering the work performed by AcSEC during the project when it deliberates the short term convergence project with International Accounting Standards on property, plant, and equipment, including depreciation.

## **Deloitte Issues *Heads Up* Article, *Narrowing Your Options! Fair Value Accounting for Share-Based Payments, Related to FASB's Exposure Draft, Share-Based Payment***

On April 13, 2004, Deloitte issued a *Heads Up* article to provide initial insights into the proposed FASB standard on share-based payment awards. The FASB issued an exposure draft, *Share-Based Payment*, on March 31, 2004, to improve the current accounting standards relating to employee stock compensation. The comment period ends June 30, 2004.

The *Heads Up* article is available on Deloitte's Web site at [www.deloitte.com](http://www.deloitte.com).

## **Recent FASB Meetings**

The summary below highlights certain tentative decisions reached or topics discussed at the FASB meetings regarding their projects. Final conclusions were not reached and further consideration is expected. Additional information is available in the FASB's weekly *Action Alert* newsletter, which is available on the FASB Web site. [Dates in parentheses indicate FASB meetings at which respective issues were discussed.]

### **Beneficial Interests in Securitized Financial Assets (March 31)**

- Discussed several alternative approaches to accounting for beneficial interests and decided to discuss the following two alternatives in more detail:

- o Require all beneficial interests to be accounted for at fair value, whether they are purchased by an investor or retained by a transferor
- o Permit an enterprise to choose to account for all beneficial interests at fair value or to:

- Account for purchased beneficial interests under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, with any identified derivatives, based on an analysis of the cash flows of the purchased beneficial interests, being accounted for as derivatives and the host being accounted for under SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and
- Account for retained beneficial interests under SFAS 133 with any identified derivatives, based on an analysis of the cash flows of the assets in the securitization transaction, being accounted for as derivatives and the host contract and other assets being accounted for under applicable GAAP.

In addition, the FASB directed the staff to investigate accounting for retained beneficial interests at fair value and separately accounting for an embedded credit liability in a securitization transaction at fair value.

#### Business Combinations: Purchase Method Procedures (March 24, April 7)

- Discussed certain accounting issues related to the assumption of short-duration insurance contract claims in a business combination, and the post-acquisition accounting for assets and liabilities arising from insurance contracts. (March 24)
- Discussed issues pertaining to the interrelation of its project on business combinations with (1) its project on equity-based compensation, and (2) FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* (revised December 2003). Specific items of discussion included:
  - o Determining whether “replaced equity awards” (e.g., outstanding awards issued by the acquiree, such as employee stock options, that are replaced by the acquirer as part of a business combination) should be treated as purchase consideration or as a separate compensation arrangement of the acquirer, and the appropriate accounting for such awards.
  - o Determining whether and how to conform the initial measurement guidance in FIN 46(R) and the measurement guidance in the draft of the proposed Statement on business combinations. (April 7)

#### Equity-Based Compensation (March 16)

- Discussed certain issues related to the Exposure Draft for Share-Based Payment. This Exposure Draft, *Share-Based Payment—an amendment of Statements No. 123 and 95*, ultimately was issued for comment on March 31, 2004, and may be downloaded from the FASB Web site. The comment deadline is June 30, 2004.

#### Fair Value Measurement (March 24)

- Discussed fair value measurement of net open positions in dealer markets in which bid and asked prices are more readily and regularly available than closing prices. The FASB clarified that fair value for net open positions should be determined by using (1) mid-market prices for the matched portion of offsetting positions, and (2) bid and asked prices, as appropriate, for net open positions.

#### Financial Performance Reporting by Business Enterprises (March 31)

- Discussed a proposed plan for this project developed by the staffs of the FASB, IASB and U.K. Accounting Standards Board. The following goals tentatively were decided on:
  - o To require a consistently presented and converged set of required primary financial statements
  - o To determine whether there is value in the notion of “recycling” items between the subtotals of net income and other comprehensive income and, if so, to determine a basis for the types of transactions and events that should be recycled and when recycling should occur in the recognition process.

#### Interpretation of SFAS No. 87, *Employers’ Accounting for Pensions* (March 31)

- Discussed remaining issues related to a proposed interpretation on measurement of “cash balance” pension plan obligations and tentatively decided that:
  - o A turnover/forfeiture assumption for nonvested participants of cash balance pension plans should continue to be considered in calculating a pension obligation for variable interest crediting rate plans
  - o Additional disclosures specific to cash balance pension plans are not necessary
  - o The effective date for all entities will be for fiscal years beginning after December 15, 2004

- o Entities should perform a new measurement upon adoption of the proposed Interpretation, and any difference in the measurement of the projected benefit obligation resulting from the adoption should be fully recognized in the income statement as a cumulative-effect-like adjustment.

### Interpretation of Statement 143 (April 7)

- Discussed and tentatively concluded that SFAS No. 143, *Accounting for Asset Retirement Obligations*, requires an entity to recognize a liability for a legal obligation to perform asset retirement activities when the retirement of the asset is conditional on a future event. Any uncertainty with respect to if, and when the asset will be retired, should be factored into the measurement of the fair value of the liability. In addition, the FASB decided that the proposed Interpretation should be effective for financial statements issued for fiscal years ending after December 15, 2005, and that the transition requirements should be consistent with SFAS 143. The FASB expects to issue an exposure draft in the second quarter of 2004.

### Mortgage Servicing Rights (March 31)

- Discussed and tentatively concluded that fair value is the appropriate measurement attribute for mortgage servicing rights and possibly for other types of servicing rights. The Board also directed the staff to investigate the feasibility of a separate project to permit, but not require, entities to account for financial instruments and similar instruments at fair value (similar to the fair value option in IAS 39, *Financial Instruments: Recognition and Measurement*).

### Loan Commitments (March 31)

- Decided to remove the loan commitments project from its agenda, in light of the issuance of SEC Staff Accounting Bulletin No. 105, *Application of Accounting Principles to Loan Commitments*.

### Qualifying Special-Purpose Entities and Isolation of Transferred Assets (March 24)

- Decided to hold a public roundtable discussion regarding the impact of setoff rights on sale accounting for transferred financial assets and directed the FASB staff to create a document summarizing their understanding of legal isolation issues, and to post that document on the FASB Web site to provide constituents with the opportunity to comment. This [document](#) is now available on the FASB's Web site. The comment deadline is May 10, 2004.

### Ratification of EITF consensuses (March 31)

- Discussed and ratified the following EITF Issues consensuses:

- o Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*
- o Issue No 03-6, *Participating Securities and the Two-Class Method Under FASB Statement No. 128*, Earnings Per Share
- o Issue No. 03-16, *Accounting for Investments in Limited Liability Companies*
- o Issue No. 04-2, *Whether Mineral Rights Are Tangible or Intangible Assets* (subject to the finalization of a FASB-directed FSP to resolve the inconsistency between the EITF's consensus and SFAS 141 and SFAS 142) [See [proposed FSPs FAS 141-a and 142-a](#)]
- o Issue No. 04-3, *Mining Assets: Impairment and Business Combinations*.

### Revenue Recognition (March 16)

- Discussed (1) clarifications of certain revenue recognition principles considered at previous FASB meetings and their related implementation guidance, (2) issues related to the initial fair value measurement of performance obligations, and (3) the nature of obligations to be included in the scope of the standard on revenue recognition. The following tentative conclusions were reached:
  - o The general standard on revenue recognition should include implementation guidance to clarify the term *customary business practice* as it is used in one of the standard's recognition principles.
  - o Explanatory guidance, including the definition of a contract, should be included in the standard to emphasize that enforceability is a necessary characteristic of a contract. However, the Board decided that it would not provide guidance on enforceability of contractual rights and obligations across legal jurisdictions.
  - o The general standard should include implementation guidance to clarify that a contract does not have to be worthy of enforcement in order to give rise to assets and liabilities.
  - o Recognition Principle #7 should be withdrawn from the model and reconsidered once further progress has been made on the application of the recognition and measurement principles.
  - o Only legally enforceable obligations (contractual and noncontractual) should be included in the scope of the revenue recognition standard.

The Board also confirmed its previous decision that performance obligations should be measured based on the price that the reporting entity would have to pay a third party to assume responsibility for performing all of its remaining obligations (that is, the "layoff price").

## Short-Term Convergence: Income Taxes (March 16)

- Discussed scope of project and tentatively decided the following:
  - o Scope exceptions to SFAS No. 109, *Accounting for Income Taxes*, should be outside the project's scope
  - o Certain differences between SFAS 109 and IAS 12, *Income Taxes (revised 2000)*, such as goodwill, leveraged leases, and share-based payments, should not be considered in this project
  - o Certain exceptions to the comprehensive deferred tax asset and liability recognition principle of SFAS 109 are to be included in the scope of the project
  - o Certain structural differences between SFAS 109 and IAS 12, and other application and implementation issues are to be included in the scope of the project.

## Short-Term Convergence: Liability Classification (March 24)

- Discussed expanding the scope of this project to include a fundamental reconsideration of the definitions "working capital" and "current assets" in Chapter 3A, "Working Capital-Current Assets and Current Liabilities," of ARB No. 43, *Restatement and Revision of Accounting Research Bulletins*. The FASB tentatively decided that Chapter 3A will be replaced entirely and modernized, and that the reconsideration of the definitions of "working capital" and "current assets" will be undertaken as part of the financial performance reporting by business enterprises project.

## FASB Project Summaries and Meeting Minutes

Project summaries maintained by the FASB staff, [handouts](#) distributed at each meeting, [FASB meeting minutes](#), and [summaries](#) of FASB meetings and recent actions are available on the FASB's Web site.

Further information about the FASB can be found on the FASB's Web site, [www.fasb.org](http://www.fasb.org).

*Conclusions of the FASB are subject to change at future Board meetings and generally do not affect current accounting requirements until an official position (Statement or Interpretation) is issued. Official positions of the FASB are determined only after extensive deliberation and due process, including a formal vote by written ballot to issue a Statement or Interpretation. The FASB Staff's guidance (FASB Staff Positions) is proposed after the Board's review, and after being exposed for public comment, becomes final if a majority of the Board does not object.*

## AICPA Developments

### **AICPA Issues Technical Practice Aid 6930.05, Sale of Real Estate Investments Held by Employee Benefit Plans and Discontinued Operations**

On April 12, 2004, the AICPA issued TPA 6930.05 to provide guidance to employee benefit plans on how to account for an investment in real estate (that generates rental income and operating expenses), that has been disposed of or is held for sale. The TPA states that there is no reason for employee benefit plans to distinguish between continuing and discontinued operations, because their financial statements do not show a statement of operations or activities. A real estate investment in an employee benefit plan should be carried at fair value and the related income/expenses and net appreciation/depreciation should be included in the statement of changes in financial status or statement of changes in net assets available for benefits.

TPA 6930.05 is available on the AICPA's Web site. This TPA, like all TPAs, has not been approved, disapproved, or otherwise acted upon by any senior technical committee of the AICPA. Although it may provide useful guidance, it is nonauthoritative and does not establish new GAAP.

Further information about the AICPA can be found on the AICPA's Web site, [www.aicpa.org](http://www.aicpa.org).

## SEC Developments

### **SEC Issues Proposed Rule: Use of Form S-8 and Form 8-K by Public Shell Companies**

On April 15, 2004, the SEC issued a proposed rule and form amendments relating to public shell companies that is intended to protect investors by deterring fraud and abuse in the securities market through the use of shell companies. The rule would assure that investors in shell companies that acquire operations or assets have access, on a timely basis, to the same kind of information as is available to investors in public companies with continuing operations. A "shell company" is defined in the proposal as a company with no or nominal operations, and with no or nominal assets, or assets consisting solely of cash and cash equivalents.

The proposed rule would prohibit shell companies from using Form S-8 and require a public shell company, when obligated to report a corporate event on Form 8-K that causes it to cease being a shell company, to include the same type of information as it would be required to file to register a class of securities under the Securities Exchange Act of 1934. The proposed amendments to Form S-8 will allow a company that ceases to be a shell company to use Form S-8, to register



securities 60 days after it has filed information equivalent to the information filed by companies registering a class of securities under the Securities Exchange Act of 1934.

The [related correspondence](#) is available on the SEC's Web site. The comment period ends June 7, 2004.

## SEC Publishes PCAOB Standards for Comment

The SEC has published for comment the following PCAOB rules:

- Auditing Standard No. 2, *An Audit of Internal Control Over Financial Reporting Performed in Conjunction With an Audit of Financial Statements* [Comments due by May 17, 2004]
- Auditing Standard No. 1, *References in Auditors' Reports to the Standards of the Public Company Accounting Oversight Board* [Comments due by April 30, 2004].

The [Standards](#) are available on the SEC's Web site.

Further information about the SEC can be found on the SEC's Web site, [www.sec.gov](http://www.sec.gov).

## PCAOB Developments

### PCAOB Forms Standing Advisory Group

On April 15, 2004, the PCAOB formed the Standing Advisory Group to assist the Board in carrying out its standard setting responsibilities. The Group is composed of 30 individuals with expertise in areas such as accounting, auditing, finance, etc., and will provide guidance to the Board on standard setting priorities and policy implications of existing and proposed standards.

The [related press release](#) is available on the PCAOB's Web site.

Further information about the PCAOB can be found on the PCAOB's Web site, [www.pcaobus.org](http://www.pcaobus.org).

## IASB Developments

### IASB Issued Exposure Draft to Amend IAS 39, *Financial Instruments: Recognition and Measurement*

On April 21, 2004, the IASB issued an exposure draft to amend IAS 39 to address concerns that the fair value option provided by IAS 39 (as revised) is being applied inappropriately by some entities. The exposure draft proposes to limit the financial assets and financial liabilities to which the option may be applied, while preserving the key benefits of the option.

The Board decided to achieve this by:

- Limiting the types of financial assets and financial liabilities to which the option may be applied to the following five specified categories:
  - o Financial assets and financial liabilities that contain embedded derivatives
  - o Financial liabilities whose cash flows are contractually linked to the performance of assets that are measured at fair value
  - o Cases when the exposure to changes in the fair value of the financial asset or financial liability is substantially offset by the exposure to the changes in the fair value of another financial asset or financial liability, including a derivative
  - o Financial assets other than loans and receivables
  - o Items that other IASB standards allow or require to be designated as at fair value through profit or loss.
- Requiring that the option may be applied only to financial assets and financial liabilities whose fair value is verifiable. The fair value of a financial asset or financial liability would be verifiable if and only if the variability in the range of reasonable fair value estimates made in accordance with IAS 39 is low. The proposal that fair value must be verifiable would apply only when the fair value option is used. It is a stricter test (i.e., one that more items will fail) than that of "reliably measured" which applies to items classified as held-for-trading, derivatives and available-for-sale financial assets.

A [related press release](#) is available on the IASB's Web site. The comment period ends July 21, 2004.

### IASB Appoints Jan Engstrom to the IASB

On April 20, 2004, Jan Engstrom was appointed to the IASB, effective May 1, 2004. Mr. Engstrom will succeed Harry Schmid in a full-time preparer position. His term will expire on June 30, 2009.

A [related press release](#) is available on the IASB's Web site.

Further information about the IASB can be found on the IASB's Web site, [www.iasb.org](http://www.iasb.org).

## Appendix: Abbreviations

<b>AcSEC</b>	Accounting Standards Executive Committee	<b>IFAC</b>	International Federation of Accountants
<b>AICPA</b>	American Institute of Certified Public Accountants	<b>IFRIC</b>	International Financial Reporting Interpretations Committee
<b>APB</b>	Accounting Principles Board	<b>IFRS</b>	International Financial Reporting Standards
<b>ARB</b>	Accounting Research Bulletin	<b>PCAOB</b>	Public Company Accounting Oversight Board
<b>EITF</b>	Emerging Issues Task Force	<b>MD&amp;A</b>	Management's Discussion & Analysis
<b>FASB</b>	Financial Accounting Standards Board	<b>SAB</b>	Staff Accounting Bulletin
<b>FIN</b>	FASB Interpretation	<b>SEC</b>	Securities and Exchange Commission
<b>FSP</b>	FASB Staff Position	<b>SFAS</b>	Statement of Financial Accounting Standards
<b>GAAP</b>	Generally Accepted Accounting Principles	<b>SOP</b>	Statement of Position
<b>GASB</b>	Governmental Accounting Standards Board	<b>TPA</b>	Technical Practice Aid
<b>IAS</b>	International Accounting Standards		
<b>IASB</b>	International Accounting Standards Board		

### Deloitte Accounting Research Tool Available

Deloitte is making available, on a subscription basis, access to its online library of accounting and financial disclosure literature. Called the Deloitte Accounting Research Tool (DART), 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 manual and other interpretative accounting guidance.

Updated every business day, DART has an intuitive design and navigation system which, together with its powerful search features, enable users to quickly locate information anytime, from any computer. Additionally, DART subscribers receive periodic e-mails highlighting recent additions to the DART library.

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

Prepared by Deloitte's National Office Accounting Standards and Communications Group. For further information, contact your local Deloitte office.

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