

# Accounting Roundup

March 16, 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 Proposed FSP FAS 129-a, Disclosure Requirements under FASB Statement No. 129, Disclosure of Information about Capital Structure, Relating to Contingently Convertible Financial Instruments**

On January 26, 2004, the FASB posted to its website a proposed FSP to address constituents' concerns about inconsistencies in disclosures of contingently convertible financial instruments, including those containing contingent conversion requirements that have not been met and are not otherwise required to be included in the calculation of diluted earnings per share (EPS). FSP FAS 129-a would require disclosure of:

- Significant terms of the conversion features of the contingently convertible financial instrument to enable financial statement users to understand the circumstances of the contingency and the potential impact of conversion.
- Whether shares of contingently convertible financial instruments are included in diluted EPS, and the reasons why or why not.
- The terms (including settlement) of any derivative transactions entered into in connection with the issuance of the contingently convertible financial instruments, how those transactions relate to the contingently convertible instrument, and the number of shares underlying the derivatives.

The guidance would be effective for interim financial statements issued after the final FSP is posted to the FASB's website and applies to all existing and newly created financial instruments. The comment deadline for this proposal is March 26, 2004.

FSP FAS 129-a is available on the FASB's website at [http://www.fasb.org/fasb\\_staff\\_positions/prop\\_fsp\\_fas129-a.pdf](http://www.fasb.org/fasb_staff_positions/prop_fsp_fas129-a.pdf).

### **Recent FASB Meetings**

The FASB discussed and reached certain tentative conclusions on the following projects. Final conclusions were not reached and further consideration is expected. The summary below highlights certain tentative decisions reached or topics discussed. Additional information is available in the FASB's weekly *Action Alert* newsletter, which is available on the FASB website at

<http://www.fasb.org/action>. [Note: dates in parentheses indicate FASB meetings at which respective issues were discussed.]

### **Business Combinations (February 25)**

- Discussed proposed revisions to SFAS No. 141, *Business Combinations*, and tentatively concluded that:
  - o The total value of consideration exchanged and the fair value of each major class of consideration should be disclosed.
  - o Existing U.S. GAAP should be followed for assets acquired or liabilities assumed for leases in a business combination.
  - o The proposed amendment to SFAS No. 109, *Accounting for Income Taxes*, should be applicable to any deferred tax valuation allowance resulting from a business combination regardless of the consummation date of that combination.
  - o Any benefit arising from excess tax goodwill should be recorded as a deferred tax asset at the acquisition date.
  - o Assets and liabilities that, prior to the issuance of the revised Statement, were not required to be recognized separately from goodwill should not be assigned a portion of the fair value of the reporting unit to determine the implied fair value of goodwill when performing an impairment assessment.
  - o The definition of a business should be revised, and guidance in FIN No. 46(R), *Consolidation of Variable Interest Entities—an Interpretation of ARB No. 51*, should be revised to conform to the new definition.

The FASB also directed its staff to explore conforming the initial measurement guidance in FIN 46(R) to the revised Statement and to work with the IASB to clarify which assets and liabilities should be included as part of the joint business combinations project.

### **Equity-Based Compensation (EBC) (February 11, February 18)**

- Discussed the cost-benefit procedures and analyses performed to date, concluded that an exposure draft for EBC should be prepared, and authorized the FASB staff to proceed in drafting the exposure draft. (February 11)
- Discussed various issues identified in an external review of a draft of the proposed Statement. Tentative conclusions were reached for the following areas (not all-inclusive):
  - o Specified the accounting for certain awards containing service and/or performance conditions and determined whether specified activities (e.g., repricing) should be treated as an award modification or cancellation
  - o Clarified the interaction of the proposed Statement with SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity*

- o Determined that the entire cost of an award should be accounted for as pertaining to future service or performance if vesting of the award requires future service or satisfaction of performance conditions, and the vesting features are substantive
- o Determined that award reconveyances should be accounted for as cancellations
- o Eliminated the notion that multiple award modifications would automatically trigger variable accounting. (February 18)

### **Fair Value Measurement (February 25)**

- Discussed the comment period deadline for the proposed Statement and the timing for issuance of the exposure draft. In addition, discussed transition approaches for financial instruments and fair value disclosures.

### **Financial Instruments: Liabilities and Equity (February 18)**

- Discussed and reached several tentative conclusions regarding how to express the distinction between equity and liabilities and assets in conceptual, definitional terms and whether there is a need for a hierarchy of criteria. The FASB also continued to discuss certain unresolved issues involving "simple instruments," including:
  - o Determining whether an obligation exists
  - o Mandatorily redeemable share issues
  - o Certain unconditional rights to receive a variable number of shares
  - o "Shares" that include or are tied to unconditional rights to receive assets.

### **Interpretation of FASB 87 (February 11)**

- Discussed a revised definition of a "cash balance pension plan" and generally agreed that the proposed definition is satisfactory for the purposes of the project.

### **Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (February 11, February 18, February 25)**

- Discussed the federal subsidy provided under the Act and tentatively concluded that the subsidy should be accounted for as a component of net periodic postretirement benefit cost. (February 11)
- Discussed accounting for the federal plan-sponsor subsidy provided by the Act within the context of SFAS No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*, and tentatively concluded that:

- o The effect of the subsidy on benefits attributable to past service should be treated as an actuarial gain.
- o The effect of the subsidy on benefits attributable to future service should be recognized as a reduction in future service cost.
- o The effect of plan amendments that cause the plan to become actuarially equivalent, as defined by the Act, together with the effects of the subsidy should be combined into a single measurement. If the effect reduces the accumulated postretirement benefit obligation (APBO), it should be treated as an actuarial gain; if the effect increases the APBO, it should be treated as a prior-service cost associated with the plan amendment.
- o The effect of plan amendments that cause a plan to cease being actuarially equivalent should be recognized as a negative plan amendment as of the date the amendment is adopted and should be accounted for based on the APBO that has been reduced by the actuarial gain attributable to the subsidy (measured as of the date of the Act's enactment, December 8, 2003).
- o The tax-exempt nature of the subsidy should be reflected for income tax accounting when the subsidy is recognized as a reduction to accrued postretirement benefit cost.  
(February 18)

- Discussed and tentatively concluded that a plan sponsor with significant prescription drug costs will be required to assess as of the date of the Act's enactment (December 8, 2003) whether the plan's prescription drug benefit is at least "actuarially equivalent" to the benefit provided under Medicare Part D. In addition, discussed the appropriate accounting if actuarial equivalency could not be determined for some period of time and proposed transition guidance and implementation dates. The Board also tentatively agreed with certain disclosure requirements proposed by the FASB staff. (February 25)

### **Qualifying Special-Purpose Entities (QSPEs) (February 11)**

- Discussed issues related to the legal-isolation criterion included in SFAS 140 and whether transfers of undivided interests in financial assets must be accomplished using a QSPE in order to receive sale accounting treatment.

### **Revenue Recognition (February 18)**

- Discussed and reached several tentative conclusions on issues surrounding four main topics:
  - o Use of the term "conditional rights and obligations" in the project
  - o Possible conflicts between decisions reached in the fair value measurement project and decisions reached on measuring performance obligations in the revenue project

- o Alternative approaches to completing the general revenue recognition standard and subsequent application guidance
- o Draft recognition and measurement principles that might be included in general standard.

### **FASB Project Summaries and Meeting Minutes**

Project summaries maintained by the FASB staff are available on the FASB's website at <http://www.fasb.org/project>. The handouts distributed at each meeting are available on the FASB's website at [http://www.fasb.org/board\\_handouts/index.shtml](http://www.fasb.org/board_handouts/index.shtml). The FASB meeting minutes are available at [http://www.fasb.org/board\\_meeting\\_minutes/board\\_meeting\\_minutes.shtml](http://www.fasb.org/board_meeting_minutes/board_meeting_minutes.shtml). Summaries of FASB meetings and recent actions are available at <http://www.fasb.org/action>.

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

*Note: 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.*

### **SEC Developments**

#### **SEC Issues Final Rule, Management's Report on Internal Control over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports—An Extension of Compliance Dates**

On February 24, 2004, the SEC issued a final rule extending the compliance dates for the Securities Exchange Act of 1934 amendments adopted on June 5, 2003, pursuant to Section 404 of the Sarbanes-Oxley Act of 2002. The amendments require a company to include a report by management on the company's internal controls over financial reporting in its annual report along with the accompanying auditor's report. As adopted, the final rule requires a company that is an "accelerated filer" (as defined) to begin to comply with the amendments for its first fiscal year ending on or after November 15, 2004. A nonaccelerated filer must comply with the amendments for its first fiscal year ending on or after July 15, 2005. In addition, the compliance dates have been similarly extended for related requirements regarding evaluation of internal control over financial reporting and management certification requirements, including certification and related requirements applicable to registered investment companies.

A press release on this matter is available on the SEC's website at <http://www.sec.gov/news/press/2004-21.htm>. The final rule is available on the SEC's website at <http://www.sec.gov/rules/final/33-8392.htm>.

## **SEC Issues Staff Accounting Bulletin No. 105, Loan Commitments Accounted for as Derivative Instruments**

On March 9, 2004, the SEC released SAB 105, which summarizes the views of the SEC staff regarding the application of generally accepted accounting principles to loan commitments accounted for as derivative instruments. The effective date for SAB 105 is March 31, 2004.

A press release on this matter is available on the SEC's website at <http://www.sec.gov/news/press/2004-28.htm>. The SAB is available on the SEC's website at <http://www.sec.gov/interps/account/sab105.htm>.

## **SEC Issues Amendments to Form 8-K and Proposes Amendments to Form 20-F and Fund Manager Disclosure Requirements**

On March 11, 2004, the SEC adopted amendments to Form 8-K. The amendments add eight new disclosure items to Form 8-K, transfer two items to the current report from the periodic reports, and expand two existing disclosure items. In addition, the amendments provide investors with timelier disclosure by replacing the current five business and 15 calendar-day Form 8-K deadlines with a new four-business-day deadline. Compliance with the amendments will be required as of August 23, 2004.

In addition, the SEC proposed amendments to Form 20-F that would affect foreign private issuers that change their basis of accounting to international standards (IFRS). Under the proposal, companies that publish IFRS financial statements for the first time for any financial year beginning no later than January 1, 2007 would be allowed to include only two years of audited financial statements in their SEC filings. Additional disclosures would also be required. This proposal's comment period is open for 30 days following publication in the *Federal Register*.

The SEC also proposed amendments to its forms that are designed to improve the disclosure that mutual funds and other registered management investment companies provide about their portfolio managers. These proposals are intended to provide greater transparency regarding portfolio managers, their incentives in managing a fund, and the potential conflicts of interest that may arise when they also manage other investment vehicles. This proposal's comment period is open for 60 days following publication in the *Federal Register*.

A press release summarizing the 8-K amendments and the proposals is available on the SEC's website at <http://www.sec.gov/news/press/2004-31.htm>.

Further information about the SEC can be found on the SEC's website at <http://www.sec.gov>.

## **PCAOB Developments**

### **PCAOB Approves Standard, An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statement, and Other Rules**

On March 9, 2004, the PCAOB approved an auditing standard that addresses both the work required to audit internal controls over financial reporting and the relationship between that audit and the audit of financial statements. The rule was issued in accordance with Sections 404(b) and 103 of the Sarbanes-Oxley Act of 2002, which directed the PCAOB to establish professional standards for the auditing of internal controls.

In addition, the Board changed the registration deadline for non-US accounting firms to July 19, 2004.

The above rules will be submitted to the SEC for final approval, as required by the Sarbanes-Oxley Act.

A related press release is available on the PCAOB's website at [http://www.pcaobus.org/pcaob\\_news\\_03-09-04.asp](http://www.pcaobus.org/pcaob_news_03-09-04.asp).

Further information about the PCAOB can be found on the PCAOB's website at <http://www.pcaobus.org/default.asp>.

## **International Developments**

### **IASB Issues Final Standard, IFRS No. 2, Share-based Payment**

On February 19, 2004, the IASB issued IFRS 2 to address accounting for share-based transactions, including grants of share options to employees. The IASB issued the standard to improve the quality, neutrality, transparency, and comparability of financial statements that follow IFRS by providing explicit guidance on how to account for share-based payments, the use of which has expanded greatly in recent years. IFRS 2 requires an entity to reflect in its profit or loss and financial position the effects of share-based payment transactions, including expenses associated with transactions in which share options are granted to employees. Measurement principles and requirements are specified in the standard for the following types of share-based payments:

- Equity-settled share-based payment transactions in which the entity receives goods or services as consideration for equity instruments of the entity (including shares or share options)
- Cash-settled share-based payment transactions in which the entity acquires goods or services by incurring liabilities to the supplier of those goods or services for amounts that are based on the price (or value) of the entity's shares or other equity instruments of the entity
- Transactions in which the entity receives or acquires goods or services and the terms of the arrangement



provide either the entity or the supplier of those goods or services with a choice of whether the entity settles the transaction in cash or by issuing equity instruments.

The requirements in IFRS 2 replace the disclosure requirements in IAS No. 19, *Employee Benefits*. IFRS 2 is effective for annual periods beginning on or after January 1, 2005. Earlier application is encouraged, and an entity electing to apply the IFRS before January 1, 2005 must disclose that fact.

A related press release is available on IASB's website at [http://www.iasb.org/news/press.asp?showPageContent=no&xml=10\\_84\\_30\\_19022004.htm](http://www.iasb.org/news/press.asp?showPageContent=no&xml=10_84_30_19022004.htm).

### **Proposed IFRIC D5, Applying IAS 29, Financial Reporting in Hyperinflationary Economies, for the First Time, Is Released**

On March 11, 2004, the IFRIC issued proposed IFRIC D5, which proposes guidance on how an entity should restate its financial statements in the first year it identifies the existence of hyperinflation in the economy of its functional currency. The proposed guidance addresses practice issues that have arisen regarding the initial application of hyperinflationary accounting, including calculation of deferred tax balances and how to restate comparatives. The proposal requires an entity to apply IAS 29 in the first year in which the existence of hyperinflation is identified as if it had always applied the standard. The draft Interpretation also explains that if detailed records of the acquisition dates of items of property, plant, and equipment are not available or capable of estimation, an independent professional assessment of the fair value of the items should be used as the basis of their restatement. The comment deadline for this proposal is May 14, 2004.

A related press release is available on IASB's website at [http://www.iasb.org/news/index.asp?showPageContent=no&xml=10\\_98\\_25\\_11032004\\_10032005.htm](http://www.iasb.org/news/index.asp?showPageContent=no&xml=10_98_25_11032004_10032005.htm).

### **Recent IASB Meeting**

The IASB discussed the following topics at its February 18-20 meeting:

- Accounting and Financial Reporting Standards for Small and Medium Size Entities
- Business Combinations (Phase II)
- Consolidation
- Multiemployer Plans (draft IFRIC Interpretation)
- Financial Instruments—Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk
- Financial Instruments—Issues Surrounding the Fair Value Option in IAS No. 39, *Financial Instruments: Recognition and Measurement*
- Revenue Recognition
- Postemployment Benefits
- Insurance Contracts

- Short-Term Convergence—Asset Disposals and Discontinued Operations
- Short-term Convergence—Withdrawal of IAS No. 20, *Government Grants and Disclosure of Government Assistance*.

A summary of the February 2004 IASB meeting is available on the IASB's website at [http://www.iasb.org/uploaded\\_files/documents/8\\_133\\_upd\\_0402.pdf](http://www.iasb.org/uploaded_files/documents/8_133_upd_0402.pdf). The observer notes and IASB staff presentations made at the meetings are available on the IASB's website at <http://www.iasb.org/meetings/0402.asp>. A summary of IASB meeting decisions and discussions is also available on Deloitte's IAS Plus website at <http://www.iasplus.com/agenda/0402.htm>.

The next IASB meeting is scheduled for March 17-19, 2004.

Further information about the IASB can be found on its website at <http://www.iasb.org> and on the IAS Plus website at <http://www.iasplus.com/index.htm>.

*Note: Conclusions of the IASB are subject to change at future Board meetings and generally do not affect current accounting requirements for entities that apply IASB standards until an official position (IFRS or Interpretation) is issued. Official positions of the IASB are determined only after extensive deliberation and due process, including a formal vote by written ballot to issue an IFRS or Interpretation.*

## **Other Developments**

### **FEI CEO'S Top Financial Reporting Issues for 2004**

In the January/February 2004 *Financial Executives International (FEI) Magazine*, the FEI's president and CEO offered a list of financial reporting issues that require special attention during 2004. The 11 issues are:

- Internal controls
- Variable Interest Entities (VIEs)
- Pension disclosures
- MD&A guidance
- Revenue recognition
- Off-balance-sheet arrangements disclosures
- Embrace transparency
- Audit committee governance
- Financial instruments with characteristics of both liabilities and equity
- Stock options
- International convergence.

The article is posted on FEI's website at [http://www.fei.org/mag/articles/1-2004\\_fr\\_dom.cfm](http://www.fei.org/mag/articles/1-2004_fr_dom.cfm).

# Appendix:

## Abbreviations

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

### 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 <http://www.deloitte.com/us/dart>.

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