

June 30, 2009

Accounting

Amendments to Statement No. 140 Issued

The Financial Accounting Standards Board (FASB) has published FASB Statement No. 166, *Accounting for Transfers of Financial Assets*, which is a revision to Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. Statement No. 166 eliminates the concept of a "qualifying special-purpose entity" from Statement No. 140 and removes the exception from applying FASB Interpretation (FIN) No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, to qualifying special-purpose entities. As a result, most securitization entities that previously met the requirements of a qualifying special-purpose entity under Statement No. 140 that are variable interest entities would now be required to be evaluated under the revised guidance in the amendment to FIN 46(R), which is discussed in the following article. Statement No. 166 also:

- Clarifies that the objective of paragraph 9 of Statement No. 140 is to determine whether a transferor and all of the entities included in the transferor's financial statements being presented have surrendered control over transferred financial assets.
- Modifies the financial-components approach used in Statement No. 140 and limits the circumstances in which a financial asset, or portion of a financial asset, should be derecognized when the transferor has not transferred the entire original financial asset to an entity that is not consolidated with the transferor in the financial statements being presented and/or when the transferor has continuing involvement with the transferred financial asset.
- Defines the term *participating interest* to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale. If the transfer does not meet those conditions, a transferor should account for the transfer as a sale only if it transfers an entire financial asset or a group of entire financial assets and surrenders control over the entire transferred asset(s) in accordance with the conditions in paragraph 9 of Statement No. 140, as amended by Statement No. 166.
- Removes the special provisions for guaranteed mortgage securitizations in Statement No. 140 and Statement No. 65, *Accounting for Certain Mortgage Banking Activities*, to require those securitizations to be treated the same as any other transfer of financial assets within the scope of Statement No. 140, as amended by Statement No. 166.
- Requires that a transferor recognize and initially measure at fair value all assets obtained (including a transferor's beneficial interest) and liabilities incurred as a result of a transfer of financial assets accounted for as a sale.
- Requires enhanced disclosures to provide financial statement users with greater transparency about transfers of financial assets and a transferor's continuing involvement with transferred financial assets.

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Statement No. 166 is effective at the beginning of a reporting entity's first fiscal year that begins after November 15, 2009. Earlier application is prohibited.

The Statement is available in full at <http://www.fasb.org>.

Amendments to FIN 46(R) Issued

The Financial Accounting Standards Board (FASB) has published FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R)*. This Statement amends FASB Interpretation (FIN) No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, to require an enterprise to perform an analysis to determine whether the enterprise's variable interest or interests give it a controlling financial interest in a variable interest entity (VIE). This analysis identifies the primary beneficiary of a VIE as the enterprise that has both (a) the power to direct the activities of a VIE that most significantly impact the entity's economic performance, and (b) the obligation to absorb losses of the entity that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE. Additionally, Statement No. 167 requires an enterprise to assess whether it has an implicit financial responsibility to ensure that a VIE operates as designed when determining whether it has the power to direct the activities of the VIE that most significantly impact the entity's economic performance.

Statement No. 167 further amends FIN 46(R) to:

- Require ongoing reassessments of whether an enterprise is the primary beneficiary of a VIE. (Before this Statement, FIN 46(R) required reconsideration of whether an enterprise is the primary beneficiary of a VIE only when specific events occurred.)
- Eliminate the quantitative approach previously required for determining the primary beneficiary of a VIE, which was based on determining which enterprise absorbs the majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both.
- Provide revised guidance for determining whether an entity is a VIE. (It is possible that application of this revised guidance will change an enterprise's assessment of which entities with which it is involved are VIEs.)
- Add an additional reconsideration event for determining whether an entity is a VIE when any changes in facts and circumstances occur such that the holders of the equity investment at risk, as a group, lose the power from voting rights or similar rights of those investments to direct the activities of the entity that most significantly impact the entity's economic performance.
- Eliminate the exception in FIN 46(R) whereby a troubled debt restructuring as defined in Statement No. 15, *Accounting by Debtors and Creditors for Troubled Debt Restructurings*, was not an event that required reconsideration of whether an entity is a VIE and whether an enterprise is the primary beneficiary of a VIE.
- Require additional disclosures about an enterprise's involvement with VIEs and any significant changes in risk exposure due to that involvement, together with how such involvement with a VIE affects the enterprise's financial statements.

Statement No. 167 is effective at the beginning of a company's first fiscal year that begins after November 15, 2009. Earlier application is prohibited. The Statement may be applied retrospectively in previously issued financial statements with a cumulative effect adjustment to retained earnings as of the beginning of the first year restated.

Statement No. 167 is available in full at <http://www.fasb.org>.

Presentation of Assets and Liabilities in Personal Financial Statements

American Institute of Certified Public Accountants (AICPA) Statement of Position No. 82-1, *Accounting and Financial Reporting for Personal Financial Statements*, states that personal financial statements should present assets at their estimated current values and liabilities at their estimated current amounts at the date of the financial statements. The SOP also defines estimated *current values* and *current amounts*.

SOP 82-1 now has been codified in Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 274, *Personal Financial Statements*, which retained the definitions of *current values* and *current amounts* for personal financial statements. However, FASB ASC 820, *Fair Value Measurements and Disclosures*, provides a definition for *fair value*. To address this inconsistency, the AICPA recently issued TIS Section 1600.04, *Presentation of Assets at Current Values and Liabilities at Current Amounts in Personal Financial Statements*, to clarify that the definitions of *current values* and *current amounts* for personal financial statements in FASB ASC 274 are not meant to be the same as *fair value* as defined in FASB ASC 820.

TIS Section 1600.04 is available in full at

http://www.aicpa.org/download/acctstd/Final_TPA_TIS_1600_04_june_4_2009.pdf.

Auditing

Proposed Standards Regarding Quality Control

In conjunction with its efforts to clarify generally accepted auditing standards for audits of nonpublic companies and to converge such standards with International Standards on Auditing (ISAs), the Auditing Standards Board of the American Institute of Certified Public Accountants (AICPA) recently issued:

- A proposed Statement on Quality Control Standards (SQCS), *A Firm's System of Quality Control (Redrafted)*, which addresses a CPA firm's responsibilities for its system of quality control for its accounting and auditing practice; and
- A proposed Statement on Auditing Standards (SAS), *Quality Control for an Audit of Financial Statements*, which specifies quality control procedures at the engagement level that assist the auditor in achieving the objectives of the quality control standards.

The proposed SQCS has been drafted using International Standards on Quality Control (ISQC) No. 1, *Quality Control For Firms That Perform Audits And Reviews Of Financial Statements, And Other Assurance And Related Services Engagements*, as a base. The proposed SQCS would supersede SQCS No. 7, *A Firm's System of Quality Control*. To reflect a more principles-based approach to standard setting, certain requirements that are duplicative of broader requirements in SQCS No. 7 have been moved to application and other explanatory material; however, the proposed SQCS does not change or expand SQCS No. 7 in any significant respect.

The proposed SAS has been drafted using ISA No. 220, *Quality Control for an Audit of Financial Statements*, as a base. The proposed SAS would supersede SAS No. 25, *The Relationship of Generally Accepted Auditing Standards to Quality Control Standards*, which currently contains no specific requirements. The proposed SAS contains requirements and application material that address specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. As these procedures are required to be established by SQCS No. 7, the proposed SAS should not result in a change to existing practice; however, the proposed SAS would strengthen existing standards by making it easier for auditors to understand and apply those quality control procedures that apply to an audit of financial statements.

It should be noted that the Public Company Accounting Oversight Board has issued a proposed auditing standard, *Engagement Quality Review*, which contains requirements relating to engagement quality control reviews that apply only to audits of issuers. Certain of these requirements are not included in the proposed SQCS or the proposed SAS.

If finalized, the proposed SQCS and the proposed SAS would be effective for audits of nonpublic financial statements for periods beginning on or after December 15, 2010. This effective date is provisional but will not be earlier than December 15, 2010.

The proposed SQCS and proposed SAS are available for comment until August 31, 2009 at http://www.aicpa.org/download/auditstd/FINAL_Proposed_SOCS_ED.pdf and http://www.aicpa.org/download/auditstd/FINAL_Proposed_SAS_OC.pdf, respectively. Bob Dohrer, National Director of Assurance Services for McGladrey & Pullen, is a member of the AICPA's Quality Control Task Force, which was responsible for redrafting the SQCS and SAS.

International

Accounting for Group Cash-Settled Share-Based Payment Transactions

The International Accounting Standards Board (IASB) has received requests for guidance on how a group entity that receives goods or services from its suppliers (including employees) should account for an arrangement whereby the entity's suppliers will receive cash payments that are linked to the price of the equity instruments of the entity and an arrangement whereby the entity's suppliers will receive cash payments that are linked to the price of the equity instruments of the entity's parent. Under either arrangement, the entity's parent has an obligation to make the required cash payments to the entity's suppliers. The entity itself does not have any obligation to make such payments.

In response to these requests, the IASB has issued amendments to International Financial Reporting Standard (IFRS) 2, *Share-based Payment*, that clarify the accounting for group cash-settled share-based payment transactions. The amendments state that an entity receiving goods or services in a share-based payment arrangement must account for those goods or services no matter which entity in the group settles the transaction, and no matter whether the transaction is settled in shares or cash. Also, the amendments clarify that in IFRS 2 a "group" has the same meaning as in International Accounting Standard 27, *Consolidated and Separate Financial Statements*, that is, it includes only a parent and its subsidiaries. Because these recent amendments to IFRS 2 incorporate guidance previously included in IFRIC 8, *Scope of IFRS 2*, and IFRIC 11, *IFRS 2—Group and Treasury Share Transactions*, the IASB has withdrawn IFRIC 8 and IFRIC 11.

The amendments to IFRS 2 state that for share-based payment transactions among group entities, in its separate or individual financial statements, the entity receiving the goods or services must measure the goods or services received as either an equity-settled or a cash-settled share-based payment transaction by assessing (a) the nature of the awards granted, and (b) its own rights and obligations. The amount recognized by the entity receiving the goods or services may differ from the amount recognized by the consolidated group or by another group entity settling the share-based payment transaction.

The entity receiving the goods or services must measure the goods or services received as an equity-settled share-based payment transaction when (a) the awards granted are its own equity instruments, or (b) the entity has no obligation to settle the share-based payment transaction. The entity must subsequently remeasure such an equity-settled share-based payment transaction only for changes in non-market vesting conditions. In all other circumstances, the entity receiving the goods or services must measure the goods or services received as a cash-settled share-based payment transaction.

If the identifiable consideration received (if any) by the entity appears to be less than the fair value of the equity instruments granted or liability incurred, typically this situation indicates that other consideration (*i.e.*, unidentifiable goods or services) has been (or will be) received by the entity. The entity must measure the identifiable goods or services received in accordance with IFRS 2. The entity must measure the unidentifiable goods or services received (or to be received) as the difference between the fair value of the share-based payment and the fair value of any identifiable goods or services received (or to be received). The entity must measure the unidentifiable goods or services received at the grant date. However, for cash-settled transactions, the liability must be remeasured at the end of each reporting period until it is settled.

The entity settling a share-based payment transaction when another entity in the group receives the goods or services must recognize the transaction as an equity-settled share-based payment transaction only if it is settled in the entity's own equity instruments. Otherwise, the transaction must be recognized as a cash-settled share-based payment transaction.

The amendments to IFRS 2 are to be applied retrospectively for annual periods beginning on or after January 1, 2010.

Fair Value Measurement: IFRS vs. U.S. GAAP

This article is the twenty-second in a series of articles that takes our readers on a journey through International Financial Reporting Standards (IFRS) with a special focus on the standards' quintessential feature: they are principles-based. In this article, we provide an overview of some of the most significant differences between IFRS and U.S. generally accepted accounting principles (GAAP) with regard to fair value measurement. Actual differences in the accounting treatment between the two frameworks depend on specific circumstances.

In November 2006 the International Accounting Standards Board (IASB) published for public comment a discussion paper setting out its preliminary views on providing consistency in the measurement of fair value when existing International Financial Reporting Standards (IFRS) require or permit its use. The starting point in developing the discussion paper was the equivalent U.S. GAAP standard, FASB Statement No. 157, *Fair Value Measurements*. In May 2009, the IASB released an Exposure Draft regarding the fair value measurement project. The proposed definition of fair value in the Exposure Draft is identical to the definition in Statement No. 157, and the supporting guidance is largely consistent with U.S. GAAP. However, some significant differences still remain. Following is a brief summary of some of the key decisions exposed:

	IFRS Exposure Draft vs. Statement No. 157	Existing IFRS
Definition of fair value	The IASB tentatively decided to define fair value as it is defined in Statement No. 157.	The current IFRS definition is based on wording that is different than that in Statement No. 157; however, it is considered to be broadly similar.
Exit price	The IASB tentatively decided to characterize fair value as an "exit price" as in Statement No. 157.	Currently, the definition in IFRS is neither explicitly an "exit price" nor an "entry price."
Transaction price and fair value at initial recognition	The IASB tentatively decided that "day one" differences are recognized in accordance with existing IFRS criteria. Under Statement No. 157 the exit price always prevails over the transaction price at all levels (Levels 1, 2, and 3). As a result, there still will be divergence in practice.	Under existing IFRS, a model-based estimate of fair value can be used instead of the transaction price if it is based entirely on observable market inputs (Levels 1 and 2).

	IFRS Exposure Draft vs. Statement No. 157	Existing IFRS
Reference market	The IASB tentatively decided that for fair value measurement purposes, transactions take place in the most advantageous market (the market in which the reporting entity would normally enter into a transaction for the asset or liability). Statement No. 157 focuses on the principal market, and in cases where there is no principal market, the reference market is the most advantageous market. As a result, there is not full convergence between the two frameworks.	Current IFRS do not contain consistent guidance. For example, in IAS 39, <i>Financial Instruments: Recognition and Measurement</i> , the reference market is the most advantageous active market to which the entity has immediate access, and in IAS 41, <i>Agriculture</i> , if an entity has access to different markets, the entity uses the most relevant one.
Blockage factor	The IASB tentatively decided to exclude blockage factors from a fair value measurement at all levels of the fair value hierarchy. Under Statement No. 157, blockage factor adjustments are expressly prohibited only at Level 1.	Blockage factor adjustment is prohibited at all levels of the fair value hierarchy.
Illiquid markets	In April 2009 the FASB issued FASB Staff Position (FSP) No. FAS 157-4, <i>Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly</i> . The IASB tentatively decided to include the guidance from the FSP in its Exposure Draft.	At present, the guidance in FSP No. FAS 157-4 is consistent with existing guidance on IFRS contained in the IASB's Expert Advisory Panel report, <i>Measuring and disclosing the fair value of financial instruments in markets that are no longer active</i> .

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