

October 6, 2009

Accounting

Applicability of Statement No. 141(R) for Reporting Periods of Less Than 12 Months

FASB Statement No. 141 (revised 2007), *Business Combinations*, fundamentally changes the manner in which an entity will account for a business combination by including, along with other significant changes, a requirement that an acquirer recognize virtually all assets acquired and liabilities assumed at 100% of their fair values, even in a partial acquisition. This Statement is to be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Earlier application is prohibited.

While determining whether Statement No. 141(R) is applicable for a business combination is straightforward in most circumstances, in some situations it is unclear. In particular, in scenarios where a company's first reporting period that begins on or after December 15, 2008 is less than twelve months it may be unclear when Statement No. 141(R) is applicable. Following are three scenarios illustrating our Firm's views on the effective date of Statement No. 141(R) in certain situations:

Scenario 1

Company A is created on April 1, 2009 and its bylaws specify it has a September 30 fiscal year end. Therefore, September 30, 2009 will be its first year end. Company A acquires a business on June 15, 2009. We believe in this scenario that Statement No. 141(R) is applicable to this acquisition. Our interpretation of the effective date of Statement No. 141(R) is that Company A's six-month reporting period beginning April 1, 2009 and ending September 30, 2009 would be considered its first annual reporting period beginning on or after December 15, 2008. The fact that the period is less than twelve months and that Statement No. 141(R) would not be applicable for other companies with one-year reporting periods ending on September 30, 2009 is irrelevant. If the FASB's intention was for all entities with the same year ends to apply Statement No. 141(R), then the effective date would have been annual reporting periods ending on or after December 14, 2009.

Scenario 2

Assume the same facts as above except that Company A's year-end is December 31. We believe in this scenario that Statement No. 141(R) is applicable to the June 15, 2009 acquisition as Company A's nine-month reporting period beginning April 1, 2009 and ending December 31, 2009 would be considered its first annual reporting period beginning on or after December 15, 2008. See Scenario 1 for further explanation.

Scenario 3

An existing operating company (OpCo) had a December 31 year end. On February 1, 2009, OpCo changes its year end to September 30, 2009. OpCo acquires a business on June 15, 2009. We believe in this scenario that Statement No. 141(R) is applicable to the June 15, 2009 acquisition as OpCo's nine-month reporting period beginning January 1, 2009 and ending September 30, 2009 would be considered its first annual reporting period beginning on or after December 15, 2008. See Scenario 1 for further explanation.

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Updates Issued for Various Technical Corrections

The Financial Accounting Standards Board (FASB) recently issued the following Accounting Standards Updates (ASUs) to make various technical corrections to the FASB Accounting Standards Codification (ASC). These ASUs are available in full at <http://www.fasb.org> and are summarized as follows:

- ASU No. 2009-07, *Accounting for Various Topics - Technical Corrections to SEC Paragraphs*. This ASU represents technical corrections to various ASC Topics containing SEC guidance. The technical corrections resulted from external comments received, and consisted principally of paragraph referencing and minor wording changes.
- ASU No. 2009-08, *Earnings Per Share - Amendments to Section 260-10-S99*. This ASU represents technical corrections to ASC 260-10-S99, *Earnings per Share*, based on Emerging Issues Task Force (EITF) Topic D-53, "Computation of Earnings Per Share for a Period that Includes a Redemption or an Induced Conversion of a Portion of a Class of Preferred Stock," and EITF Topic D-42, "The Effect of the Calculation of Earnings per Share for the Redemption or Induced Conversion of Preferred Stock." The revisions consisted principally of formatting changes and removing out-of-date guidance.
- ASU No. 2009-09, *Accounting for Investments - Equity Method and Joint Ventures and Accounting for Equity-Based Payments to Non-Employees - Amendments to Sections 323-10-S99 and 505-50-S99*. This ASU represents a correction to ASC 323-10-S99-4, *Accounting by an Investor for Stock-Based Compensation Granted to Employees of an Equity Method Investee*, which was originally posted in the ASC incorrectly. In addition, the ASU adds to ASC 505-50-S99 the following SEC Observer comment from EITF Issue No. 00-18, "Accounting Recognition for Certain Transactions Involving Equity Instruments Granted to Other Than Employees":

"SEC registrants can expect the SEC Staff to challenge accounting by the grantee or grantor in transactions involving equity instruments granted to other than employees if their accounting does not reflect the same commitment date or similar values."
- ASU No. 2009-10, *Financial Services—Broker and Dealers: Investments—Other - Amendment to Subtopic 940-325*. This ASU codifies in ASC 940-325-S99-1 the following SEC Observer comment from EITF Issue No. 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management":

"The guidance prohibiting mark-to-market accounting for nonderivative energy trading contracts is equally applicable to brokers and dealers, as the Guide for brokers and dealers in securities does not afford brokers and dealers special treatment in that regard."
- ASU No. 2009-11, *Extractive Activities—Oil and Gas - Amendment to Section 932-10-S99*. This ASU represents a technical correction to ASC 932-10-S99-5 for the following addition to the SEC Observer comment in EITF Issue No. 90-22, "Accounting for Gas-Balancing Arrangements":

"Registrants should account for all significant gas imbalances consistently, using one accounting method. SEC registrants should disclose their method of accounting, as well as the amount of any imbalance in terms of units and value, if significant."

Proposed Revisions for Oil and Gas Accounting

The Financial Accounting Standards Board (FASB) has issued a proposed Accounting Standards Update (ASU), *Extractive Industries—Oil and Gas (Topic 932) - Oil and Gas Reserve Estimation and Disclosures*. The objective of this proposed ASU is to align the oil and gas reserve estimation and disclosure requirements of FASB ASC Topic

932 with the requirements in the SEC's final rule, *Modernization of the Oil and Gas Reporting Requirements*, which was issued on December 31, 2008. Some of the key provisions of the proposed ASU include the following:

- Expanding the definition of oil- and gas-producing activities to include the extraction of saleable hydrocarbons, in the solid, liquid, or gaseous state, from oil sands, shale, coal beds, or other nonrenewable natural resources that are intended to be upgraded into synthetic oil or gas, and activities undertaken with a view to such extraction.
- Amending the definition of proved oil and gas reserves to indicate that entities must use the average, first-day-of-the-month price during the 12-month period before the ending date of the period covered by the report rather than the year-end price, when estimating whether reserve quantities are economical to produce. Likewise, the price used to calculate the aggregate amount of (and changes in) future cash inflows related to the standardized measure of discounted future cash flows would be changed from the year-end price to the 12-month average price used in calculating proved reserves.
- Requiring that an entity disclose separately information about reserve quantities and financial statement amounts for geographic areas that represent 15 percent or more of proved reserves. In addition, Topic 932 would indicate that the quantity of reserves is not the only factor that should be considered in determining whether reserves are significant (*i.e.*, an entity would be required to consider all facts and circumstances in determining whether reserves are significant).
- Clarifying that an entity's equity method investments must be considered in determining whether it has significant oil- and gas-producing activities. Separate disclosures about amounts and quantities for consolidated and equity method investments would continue to be required, but an entity would be permitted to disclose the total of the consolidated and equity method investment amounts and quantities. Disclosures about equity method investments with significant oil- and gas-producing activities would be required in the same level of detail as is required for consolidated investments.

If finalized, the proposed amendments to Topic 932 would be effective for annual reporting periods ending on or after December 31, 2009, and would be applied prospectively as a change in estimate. Early application would not be permitted.

The proposed ASU is available for comment until October 15, 2009 at

<http://www.fasb.org/cs/ContentServer?c=Page&pagename=FASB%2FPage%2FSectionPage&cid=1175801893139>.

Auditing

Effective Enterprise Risk Oversight

On September 1, 2009, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) released a four-page paper, *Effective Enterprise Risk Oversight: The Role of the Board of Directors*, to help boards of directors strengthen their oversight of enterprise risks. This paper calls attention to COSO's *Enterprise Risk Management - Integrated Framework*, which highlights the following four areas that contribute to board oversight of enterprise risk management. In accordance with this framework, boards of directors should:

- Understand the entity's risk philosophy and concur with the entity's risk appetite - Risk appetite is the amount of risk, on a broad level, an organization is willing to accept in pursuit of stakeholder value. Because boards represent the views and desires of the organization's key stakeholders, management should have an active discussion with the board to establish a mutual understanding of the organization's overall appetite for risks.

- Know the extent to which management has established effective enterprise risk management of the organization - Boards should inquire of management about existing risk management processes and challenge management to demonstrate the effectiveness of those processes in identifying, assessing, and managing the organization's most significant enterprise-wide risk exposures.
- Review the entity's portfolio of risk and consider it against the entity's risk appetite - Effective board oversight of risks is contingent on the ability of the board to understand and assess an organization's strategies with risk exposures. Board agenda time and information packets that integrate strategy and operational initiatives with enterprise-wide risk exposures strengthen the ability of boards to ensure risk exposures are consistent with overall appetite for risk.
- Be apprised of the most significant risks and whether management is responding appropriately - Risks are constantly evolving and the need for robust information is of high demand. Regular updating by management to boards of key risk indicators is critical to effective board oversight of key risk exposures for preservation and enhancement of stakeholder value.

Effective Enterprise Risk Oversight: The Role of the Board of Directors is available in full at <http://www.coso.org/documents/COSOBoardsERM4pager-FINALRELEASEVERSION82409.pdf>.

Proposed Standard Regarding Auditing Related-Party Transactions and Disclosures

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 recently issued a proposed Statement on Auditing Standards (SAS), *Related Parties (Redrafted)*. If finalized, this proposed SAS would supersede the "Related Parties" Section of SAS No. 45, *Omnibus Statement on Auditing Standards – 1983*. (AU Section 334). Extant AU Section 334 is focused on auditing the amounts and disclosures required by accounting principles generally accepted in the United States and is centered on the provisions of FASB Statement No. 57, *Related Party Disclosures* (FASB ASC 850-10). The proposed SAS has been drafted using ISA 550, *Related Parties*, as a base and is framework neutral. Thus, the proposed SAS would include financial reporting frameworks, such as accounting principles generally accepted in the United States and International Financial Reporting Standards, as well as special-purpose frameworks. The applicability of the objectives, requirements, and definitions in the proposed SAS are irrespective of whether the framework establishes such requirements.

If finalized, 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 SAS is available for comment until December 15, 2009 at http://www.aicpa.org/download/auditstd/ED_Related_Parties.pdf.

Public Sector

Not-for-Profit Entities: Mergers and Acquisitions

On September 18, 2009, the Financial Accounting Standards Board broadcast a webcast, which discussed the key provisions of FASB Statement No. 164, *Not-for-Profit Entities: Mergers and Acquisitions*. This Statement is effective for mergers occurring on or after December 15, 2009, and acquisitions for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2009. An archived version of the one-hour webcast is available at <http://w.on24.com/r.htm?e=163023&s=1&k=C1EB5ED935BED59B47B4B1E495983A18>.