

Originally issued May 2010
Updated August 2010



More Accounting Changes Coming...

Accounting Insights is a publication of McGladrey & Pullen, LLP and should not be construed as accounting, auditing, consulting, or legal advice on any specific circumstances or facts. The contents are intended for general information purposes only. You are urged to consult your McGladrey service provider concerning your situation and any specific questions you may have.

A significant number of new accounting standards have been issued in the past five years. Some of these standards cover broad topics such as fair value, business combinations, subsequent events and consolidation, which affect most companies. Other new standards cover topics like stock options, securitizations, and industry-specific standards, which do not affect as many companies. Many “mini” projects, for example those addressed by the Financial Accounting Standards Board’s (FASB’s) Emerging Issues Task Force, have narrow scopes and are more in the nature of interpretations. Some standards have only prescribed expanded disclosures. On top of these changes is the FASB’s *Codification* (also referred to as the *Accounting Standards Codification* or ASC), which brings together all authoritative standards in one place and reorganizes all of the guidance by topic. While it has been difficult to keep pace with these significant changes, they will pale in comparison to the changes on the horizon. This **August** update outlines changes related to the lease project (page 17) as well as a discussion on page 3 of significant developments in two FASB only projects related to disclosures of credit quality and additional contingency disclosures.

A question being debated today is whether and/or when the U.S. Securities and Exchange Commission (SEC) will permit or require U.S. public companies to adopt International Financial Reporting Standards (IFRS). A further question is how any decision the SEC makes will affect private companies. In February 2010, the SEC released a statement in support of IFRS, but stated it believes more study on a number of key questions is necessary before any decisions are made. The SEC staff has developed a "work plan" covering six major topics to evaluate before any decision is made. One major subject under evaluation is measuring the progress on "convergence" between U.S. generally accepted accounting principles (GAAP) and IFRS. The theory is if the major standards are closer together or converged, the effort for conversion to IFRS will be less.

In 2002, the FASB and International Accounting Standards Board (IASB) agreed to work together to converge U.S. GAAP and IFRS. The agreement is documented in a "Memorandum of Understanding" or MOU and identifies a significant number of standards and projects to be modified/converged. Today there are at least a dozen joint FASB/IASB projects in process. The goal of each project is to replace the existing FASB and IASB guidance on the topic with a common standard. This paper discusses six of the projects that will have the biggest impact on virtually all companies, plus the planned changes to the guidance on how to measure fair value. The six projects are:

- Financial statement presentation
- Revenue recognition
- Financial instruments
- Leases
- Financial instruments with characteristics of equity
- Consolidation

The discussions on these projects reflect developments through August 2010. The long standing schedule for all of these projects was to finalize them by June 2011. That schedule was recently revised to allow constituents more time to review and comment on the exposure drafts. The revised dates will mean certain projects are not expected to be finalized until the end of 2011. The FASB held a webcast in July to report progress on the joint projects. An archived version of this webcast is available on the FASB website.

The effective dates have not been set, but there may be an extended implementation period. 2011 is still a critical date for issuing these standards. IFRS is scheduled to be adopted in a number of countries in the near term. These countries represent some of the world's largest economies. The IASB has committed that these major convergence projects will be completed and the related changes incorporated into IFRS before these countries convert to IFRS. With this aggressive schedule, the strength of the commitment to the MOU and convergence is being tested.

A number of steps need to be completed before these projects are final. Each project has already been extensively debated by the FASB and IASB. Documents were published in the past few years for preliminary feedback. Currently, there are significant differences in views between the IASB and FASB for some projects. Formal "exposure drafts" of each project will be released by the middle of 2011 for public comment.

Five exposure drafts have already been issued:

- Financial Instruments
- Statement of Comprehensive Income
- Fair Value Measurement
- Revenue Recognition
- Leases

In addition, an unusual step was taken for the Financial Statement Presentation project with the issuance of a “Staff Draft” of an exposure draft for the project. The Staff Draft allows constituents to get an early start on reviewing the comprehensive model agreed upon by the FASB and IASB. A formal exposure draft is expected to be issued in early 2011.

After feedback on these exposure drafts is evaluated, final decisions will be made by each Board and a standard issued for each project, hopefully the same standard for both U.S. GAAP and IFRS. The effective dates and transition methods will be decided after all input is considered. Because the guidance on transition generally includes retrospective application, a default assumption should be that all the new guidance will apply to existing arrangements. The disclosure requirements that have been discussed are not included in the summaries that follow, but many new requirements will likely apply.

Two significant developments related to expanded disclosures occurred in July. The first development is in response to concerns that the existing disclosure requirements about an entity’s allowance for credit losses and the credit quality of an entity’s financing receivables do not provide adequate information. The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*. This ASU requires companies to provide more information in their disclosures about the credit quality and risk exposures of their financing receivables and the credit reserves held against them. For public companies, the amendments that require disclosures as of the end of a reporting period are effective for periods ending on or after December 15, 2010. The amendments that require disclosures about activity that occurs during a reporting period are effective for periods beginning on or after December 15, 2010. For nonpublic companies, the amendments are effective for periods ending on or after December 15, 2011.

The second development responds to concerns that for years, investors and other financial statement users have been asking for more disclosures in the financial statements related to litigation and other contingencies. The current requirements are very minimal. Investors often ask the question: “Why is it we only learn after it is settled or lost how significant a claim against a company was?” On July 20, 2010, the Financial Accounting Standards Board (FASB) issued an exposure draft of a proposed Accounting Standards Update, *Contingencies—Disclosure of Certain Loss Contingencies* (the proposed ASU). The proposed ASU would require disclosure of both qualitative and quantitative information about loss contingencies that are intended to assist users of financial statements in assessing the likelihood, potential magnitude and potential timing (if known) of future cash outflows associated with loss contingencies. It also requires public companies to show a “rollforward” of the aggregate amounts for loss contingencies. The proposed effective date of the disclosures for public companies would be for fiscal years ending after

December 15, 2010. For nonpublic companies, the proposed disclosures would be effective for the first annual period beginning after December 15, 2010. For public companies, that is an unusually short time period between issuance of a standard and the effective date.

For private companies, these are “interesting” times, to say the least. In December 2009, the American Institute of Certified Public Accountants, Financial Accounting Foundation and National Association of State Boards of Accountancy announced the establishment of a “Blue-Ribbon Panel” to address how U.S. accounting standards can best meet the needs of users of private company financial statements. The formation of this panel is the most significant development in private company accounting standard setting since the “Wheat Report” in 1972 on the *Establishment of Accounting Principles*, which led to the creation of the FASB. The time is right to address the problems private companies face in accounting. The Blue Ribbon Panel is asking for public feedback on three possible approaches: (a) U.S. GAAP with exclusions for private companies—with enhancements from today’s approach, (b) U.S. GAAP—baseline GAAP with public company add-ons, or (c) separate, stand-alone GAAP based on current U.S. GAAP

We don’t know how the Blue-Ribbon Panel’s recommendations will affect these major projects for private companies. For public companies, regardless of the ultimate decisions on whether and/or when IFRS will be required, the changes to U.S. GAAP as a result of these major projects will be applicable.

Every organization should be concerned about these major projects. The new financial statement format will require the balance sheet and income statement to look more like a cash flow statement does today. The percentage-of-completion method of revenue recognition may not be available to many businesses. All leases will be capitalized. Most financial instruments, including loans and receivables, will be accounted for at fair value. Many instruments classified as equity today will be classified as liabilities in the future. The consolidation rules will change again. Major system changes will be necessary. Loan covenants may need to be modified. Buy-sell agreements may no longer make sense. Financial statement users will need substantial help to understand the changes.

The summaries in this paper are condensed and don’t discuss every aspect of each project. The FASB’s Web site, www.fasb.org, has more information on all projects. McGladrey has also written more extensive publications of a number of the proposals, available at www.mcgladreypullen.com. As the exposure drafts are issued, anyone can comment on them. The most useful comments often relate to how the changes will affect financial statement users. The FASB also needs to hear from preparers about the practical difficulties and costs companies will face to implement the new standards. Appendix B includes many of the joint projects and provides a current timetable.

Various Financial Accounting Standards Board documents and portions thereof, copyright © by the Financial Accounting Foundation, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856, are reproduced with permission. Complete copies of these documents are available from the FAF.

Financial Statement Presentation

Overview

Is the financial reporting community ready for fundamental and unprecedented changes to how financial statements look and how they are used? Everyone is going to have to answer this question as we consider the conclusions reached by the FASB and IASB in their joint project on “Financial Statement Presentation.” The overriding objective of this project is to make financial statements more relevant to users of the financial statements. Here are a few of the more significant changes that are meant to accomplish that objective:

- Including operating, investing, and financing sections or categories on the balance sheet and income statement, similar to what is currently done in the cash flow statement;
- Changing the income statement to a statement of *comprehensive* income;
- Requiring use of the direct method to present cash flows from operating activities; and
- Reconciling the beginning and ending balances for certain “important” accounts shown on the balance sheet by using a pre-set list of six different types of reconciling items.

Will these and the other changes proposed in the joint project provide more relevant information to users of the financial statements? If so, at what cost to preparers? To comply with the changes proposed in the joint project, preparers will likely incur significant costs. For example, wholesale changes to a preparer’s financial reporting system may be required to accommodate breaking information out on the balance sheet and income statement between operating, investing, and financing sections or categories. In addition to making changes to its financial reporting system, a preparer may also need to make changes to its treasury systems to accommodate using the direct method to present cash flows from operating activities. This project has significant implications to financial statement preparers above and beyond the costs associated with system changes. For example, how will compliance with debt covenants be affected by the changes proposed in this joint project? Will debt covenants have to be renegotiated and, if so, will there be a cost to these renegotiations?

The changes proposed in this project will affect all parties involved in the financial reporting process (e.g., users, preparers, auditors). Significant efforts will have to be undertaken to inform and educate all of the affected parties on the new look and feel of financial statements and how best to use them.

	Note	GROUP	2010 \$'000 (restated)
		50,161	45,421
		116	2,256
			7,344
	3	22,251	5,352
	4	1,933	12
	5	737	994
	6	579	
	7		61,379
	8	75,777	
	9		61,805
Non-current assets			112,489
Property, plant and equipment		27,790	85
Intangible assets		122,857	20,90
Subsidiaries		1,027	196.07
Investments		30,360	
Other			

Scope

The changes proposed in this project will affect the financial statements of both public and private companies in the U.S. While private companies will not have to provide the reconciliation disclosure mentioned in the “Overview,” all of the other substantive changes proposed in this project will be applicable to private companies. Only not-for-profit entities and benefit plans are exempt from the scope of this project.

Core Principles

The core principles embodied by the FASB and IASB in this project are to: (a) portray a cohesive financial picture of an entity’s activities, and (b) disaggregate information so it can be used in predicting an entity’s cash flows.

Cohesive Principle – The “cohesive” principle is primarily achieved through a common organizational structure across the financial statements. The Statement of Financial Position, Statement of Comprehensive Income and Statement of Cash Flows will each have the following sections (as appropriate): (a) Business, (b) Financing, (c) Income Taxes, (d) Discontinued Operations, and (e) Multicategory Transactions (*i.e.*, transactions that affect multiple categories, such as business acquisitions). The Business section will be further broken down into Operating and Investing categories. The Financing section on the Statement of Financial Position and Statement of Comprehensive Income will be further broken down into Debt and Equity categories. If appropriate, the Operating category within the Business section will have an Operating Finance subcategory. The categorization on the Statement of Comprehensive Income and Statement of Cash Flows is generally driven by the categorization of the related asset or liability on the Statement of Financial Position.

Disaggregation Principle – The “further disaggregation” principle is primarily achieved by requiring balances and results to be broken out into material classes of similar items. These classes may be based on function, nature, and/or measurement basis. For example, it might be appropriate to functionally break out revenue between sales of product and sales of services. It might be appropriate to further break out product revenue between wholesale and retail classes. Another level of disaggregation would come into play on the Statement of Financial Position if different measurement bases (e.g., historical cost and fair value) are used in the accounting for assets or liabilities of a certain nature. How “useful” (as defined) the disaggregated information is will play a large part in determining how much disaggregation will be needed in the financial statements.

Effects of Core Principles – The old adage “a picture is worth a thousand words” is particularly appropriate in the context of this project when trying to understand the full effect of implementing the core principles of this joint project on the financial statements. As such, included in Appendix A of this document are examples of a Statement of Financial Position and a Statement of Comprehensive Income that were included in the FASB’s *Staff Draft of an Exposure Draft on Financial Statement Presentation*. This draft was posted to the FASB’s website on July 1, 2010. When looking at these examples, the changes this joint project will bring to the financial statements are acutely apparent.

Other Key Decisions

A number of other key decisions have been reached by the FASB and IASB in this joint project. Included below are just a sampling of these decisions and what could be in store for the financial reporting community when this project is finished.

Required Components of the Financial Statements – The financial statements would include the following components: (a) Statement of Financial Position, (b) Statement of Comprehensive Income, (c) Statement of Cash Flows, (d) Statement of Changes in Equity, and (e) footnotes.

Comparative Information – An entity will be required to show comparative information for the previous period. While no action has yet been taken by the SEC with respect to the conclusions reached in this project, it is unlikely that this project will result in the SEC making any changes to the comparative financial statement requirements applicable to public companies.

Short-Term vs. Long-Term Classification – An entity will use a timeframe of one year for purposes of categorizing assets and liabilities as short-term and long-term on the Statement of Financial Position. However, an entity would classify its assets and liabilities in order of their liquidity if that presentation were more meaningful than the short-term and long-term classifications.

Operating Finance Subcategory – An Operating Finance subcategory would be included on the Statement of Financial Position and Statement of Comprehensive Income. Only items meeting specific criteria would be included in this subcategory (e.g., lease obligations and net postemployment benefit obligations).

Including Comprehensive Income on the Income Statement – The FASB and IASB have moved their conclusions with respect to including other comprehensive income on one continuous Statement of Comprehensive Income from the “Financial Statement Presentation” joint project to a separate joint project (for which an exposure draft was issued on May 26, 2010). As part of this separate joint project, the amount an entity reports as other comprehensive income will not change; however, where and how the entity presents other comprehensive income in the financial statements will change.

Foreign Currency Transaction Gains and Losses – Foreign currency transaction gains and losses will need to be reflected in the appropriate section and category within the Statement of Comprehensive Income. The appropriate section and category would be dictated by the section and category in which the underlying assets and liabilities that gave rise to the gains and losses are reflected on the Statement of Financial Position.

Extraordinary Items – An entity will no longer be allowed to classify gains and losses as “extraordinary” on the Statement of Comprehensive Income.

Beginning and Ending Cash Balances on Statement of Cash Flows – The beginning and ending cash balances shown on the Statement of Cash Flows will reflect only an entity’s cash balances and not include what is commonly referred to as cash equivalents (i.e., short-term, highly liquid investments that meet certain conditions).

Cash Flows from Operating Activities – An entity will be required to use the direct method to present cash flows from operating activities on the Statement of Cash Flows. For purposes of determining gross cash receipts and gross

cash payments to be included in the direct method of presenting cash flows from operating activities, the Staff Draft points out that such gross amounts could be determined either directly or indirectly. Even though the direct method will be used to present cash flows from operating activities, a reconciliation of operating income to operating cash flows will still have to be provided on the face of the Statement of Cash Flows (much the same as is currently done when the indirect method is used to present cash flows from operating activities).

Definitions of Operating, Investing, and Financing – While the concepts of operating, investing and financing activities are currently used in the Statement of Cash Flows, the way in which these concepts are defined will change as a result of this joint project. For example, acquisitions and dispositions of property, plant and equipment will likely fall within the Operating category of the Business section (compared to their current inclusion in the investing section of the Statement of Cash Flows).

Reconciliations for “Important” Accounts – A public company will be required to reconcile the beginning and ending balances for certain “important” accounts (as defined) shown on the Statement of Financial Position by using a pre-set list of six different types of reconciling items. The reconciliation would need to be provided for both the current and comparative periods and it would need to be accompanied by qualitative discussion.

Remeasurement Disclosures – An entity will be required to disclose information about remeasurements (as defined) and their effects on income and expense items included in the Statement of Comprehensive Income for both the current and comparative periods. The entity would have to identify the section(s), category(ies), and subcategory affected by each remeasurement.

Segment Disclosures – If otherwise required to disclose segment information, an entity will need to provide the following information for each reportable segment, regardless of whether the information is regularly reviewed by (or provided to) the Chief Operating Decision Maker, (a) income and expenses by their nature, (b) operating assets, (c) operating liabilities, and (d) operating cash flows. An entity will need to reconcile the total of the amounts shown across all reportable segments for each of these items to the consolidated totals shown for these items in the corresponding financial statement.

Differences between FASB and IASB

In general, the FASB's and IASB's decisions on this project have been well-aligned. There are only a few issues on which the FASB and IASB have reached different conclusions. One example is that private entities will be included within the scope of the FASB's project, while not being included in the scope of the IASB's project. A second example has to do with the FASB requiring income and expense information by nature for each reportable segment. The IASB is not requiring the disclosure of this information. With respect to the major decisions reached on the project, the FASB and IASB appear to be headed in the direction of issuing exposure drafts that are substantially similar to each other.

Revenue Recognition

New Revenue Standard Could Bring Complex Changes

Businesses in the professional services and manufacturing sectors could see dramatic changes to their accounting policies if a new standard for recognizing revenue proceeds as proposed.

“If you are a run-of-the-mill retailer, you’re probably not going to see that much of a change,” says Brian Marshall, a McGladrey & Pullen partner. “But for certain companies and certain types of transactions, this could lead to huge change.”

Excerpt from an article featured in Compliance Week, July 13, 2010

Overview

Revenue is a crucial number to users of financial statements in assessing a company’s performance and prospects. The revenue recognition project has an objective to clarify the principles for recognizing revenue and develop a single common revenue standard that would:

- Remove inconsistencies and weaknesses in existing revenue recognition standards and practices;
- Provide a more robust framework for addressing revenue recognition issues;
- Improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets; and
- Simplify the preparation of financial statements by reducing the number of requirements to which entities must refer.

The FASB and IASB issued an Exposure Draft on this project, *Proposed Accounting Standards Update, Revenue Recognition (Topic 605), Revenue from Contracts with Customers*, on June 24, 2010, with the comment period ending October 22, 2010.

The Boards held a webcast to provide an overview of the proposed Accounting Standards Update on July 8, 2010. An archived version of the webcast and slides are available on the FASB and IASB websites.

This guidance would be applicable to revenue resulting from an entity’s contracts with customers and would replace a significant amount of general and industry-specific revenue recognition guidance that was previously issued in individual standards. As proposed, revenue would be recognized as goods or services are transferred to a customer in an amount that reflects the consideration received or expected to be received for the goods delivered or the services performed. The approach required to apply this guidance would be as follows:

- Identify the contract(s) with the customer
- Identify the separate performance obligations in the contract
- Determine the transaction price
- Allocate the transaction price to the separate performance obligations
- Recognize revenue when each performance obligation is satisfied

Some industries and transactions may not experience any change in the timing or amount of revenue recognized. A retailer or restaurant that delivers everything to a customer at the point of sale with no return privileges will not be affected. However, a construction contractor that currently reports revenue as the contract progresses may see a dramatic shift in revenue timing.

Scope

Most contract-based revenue transactions to provide goods or services that are an output of an entity’s ordinary activities would be in the scope of this proposed new standard. Exceptions include contracts relating to financial instruments, guarantees other than product warranties, insurance or leases as well as certain nonmonetary exchanges. A contract may include multiple performance obligations, including those within the scope of this guidance and those within the scope of other guidance. In these cases, entities would be

required to account for the performance obligations within the scope of other guidance in accordance with that guidance if it specifies how to separate or measure that performance obligation. Otherwise, all of the performance obligations would be accounted for in accordance with the new proposed revenue recognition standard.

Contracts for the sale of nonfinancial assets that are not an output of an entity's ordinary activities (and hence not classified as revenue) should nonetheless follow the recognition and measurement principles of this proposed new standard.

Identify the Contract(s) with the Customer

A contract (which can be written, oral or implied) would be defined as an agreement between two or more parties that creates enforceable rights and obligations. The guidance would generally be applied on an individual contract basis but in certain cases contracts would be combined or segmented. The principle to use when determining whether to combine contracts is whether the prices in the contracts are interdependent. Conversely, an entity must separate or segment a contract when certain goods or services are priced independently from other goods or services in the same contract. These same combination and segmentation principles would be applied when there is a modification to an existing contract. If the modification is priced independently from the original contract, it would be accounted for separately. Otherwise, the modification would be accounted for with the original contract and the resulting cumulative effect would be recognized in the income statement in the period in which it occurs.

Identify the Separate Performance Obligations in the Contract

A performance obligation is defined in this project as an enforceable promise in a contract to transfer a good or service to a customer. Entities must identify each performance obligation in a contract and then determine whether they must be accounted for separately from one another. A performance obligation would be accounted for separately if the underlying goods or services are distinct from other goods or services promised in the contract. A good or service would be considered distinct from others if it is sold separately by any entity in the customer's market. Absent separate sales, a good or service could still be considered distinct if it has both a distinct function and a distinct profit margin. If goods or services are not considered distinct from other goods or services, they must be combined with other goods and services until there is a distinct bundle of goods or services. If a distinct bundle can't be identified, all goods or services would be combined into a single performance obligation.

Determine the Transaction Price

A transaction price in a contract is the probability-weighted estimate of the amount of consideration received or expected to be received from the customer that can be reasonably estimated. When determining the transaction price under the proposed guidance, an entity would start with the fixed cash consideration (if any) and adjust this amount for estimated variable consideration. The resulting amount would be further adjusted to take into consideration the risk of not collecting the consideration from the customer, the time value of money (if material), noncash consideration and consideration payable to the customer. If the transaction price can't be reasonably estimated, then it is considered to be zero until it is reasonably estimable. If only a portion of the transaction price is reasonably estimable, that portion shall be considered the transaction price. The transaction price would be updated if circumstances

change during the term of the contract. For example, a change in circumstance would be the ability to reasonably estimate a transaction price that is entirely variable subsequent to the inception of the contract. However, once an entity has an unconditional right to receive consideration as discussed in the “Presentation” section, any change in the assessment of collection risk would be recognized as other income or expense rather than an adjustment to the transaction price. In some situations (retailers or restaurants), this will not result in a change in practice, but many other industries will be challenged to implement these provisions.

Allocate the Transaction Price to the Separate Performance Obligations

If a contract has multiple performance obligations, the transaction price will need to be allocated to each performance obligation based on their standalone selling prices in relation to one another (*i.e.*, on a relative standalone selling price basis). The best evidence of the standalone selling price of a performance obligation is the observable price of the goods or services underlying the performance obligation when sold separately. If there is no separate observable price, entities would estimate the standalone selling price through the use of observable inputs, such as the good or service’s cost plus a margin or the prices at which similar goods or services are sold separately by competitors adjusted for the entity’s own cost structure and margin expectations. Any subsequent changes to the transaction price in a contract would be allocated to all performance obligations on a relative standalone selling price basis. If a change in the transaction price affects the amount allocated to a satisfied performance obligation, it should be recognized as revenue or a reduction of revenue during the period the change occurs.

Recognize Revenue when Each Performance Obligation Is Satisfied

The exposure draft requires revenue to be recognized as goods or services are transferred to a customer, which occurs when an individual performance obligation is satisfied by the transfer of control of that good or service. While not conclusive on a standalone basis or necessarily relevant for every good or service, indicators of control of a good or service being transferred include when a customer:

- Has an unconditional obligation to pay;
- Has physical possession;
- Has legal title; and
- Specifies the design or function of the good or service.

Control of a good or service may transfer at a specific point in time (*e.g.*, delivery of certain goods) or continuously (*e.g.*, performance of services). When control is transferred on a continuous basis, the method used to determine the pattern of revenue recognition for each performance obligation would be the one that best depicts the timing of the transfer of goods or services to a customer and it would need to be applied consistently. The methods utilized may include those based on inputs (such as costs incurred or labor hours expended), outputs (such as units produced or delivered) or simply the passage of time.

Onerous Performance Obligations

Performance obligations would not be remeasured after contract inception unless they are considered to be in a loss position, which has been described in this project as “onerous”. An onerous performance obligation is one in which the present value of the probability-weighted costs to satisfy the obligation are

greater than the transaction price allocated to it. In these situations, a liability would be recognized (separately from other assets and liabilities resulting from the contract) for the excess of the present value of these probability-weighted costs over the allocated transaction price. The measurement of this liability would be adjusted at each subsequent reporting period.

Costs

As currently proposed, certain costs relating to contracts with customers (that are not eligible for capitalization in accordance with other guidance) would be required to be expensed as incurred, while others would be recorded as an asset when initially incurred. The following costs would be expensed as incurred:

- Costs of obtaining a contract (e.g. sales commissions, advertising, etc.);
- Costs related to satisfied performance obligations; and
- Costs of abnormal wasted materials, labor or other resources

However, the direct costs of fulfilling a contract that are not capitalizable based on other guidance would be recorded as an asset if they generate or enhance a resource that will be used to satisfy future performance obligations, relate directly to a contract (or specific contract under negotiation), and are expected to be recovered. This asset would be amortized as the related goods or services are transferred to the customer and tested for impairment by comparing the asset's carrying amount to the transaction price allocated to the remaining performance obligations less the costs that relate directly to satisfying those performance obligations.

Presentation

A contract asset or liability should be recognized in the statement of financial position dependent upon the relationship between the entity's performance (i.e., transfer of goods or services to the customer) and the customer's performance (i.e., consideration paid to the vendor). If an entity's performance is greater than that of a customer, a contract asset should be recognized. While if a customer's performance is greater than that of the entity, a contract liability should be recognized. Furthermore, an unconditional right to receive consideration should be recorded as a receivable separately from the preceding contract asset or liability.

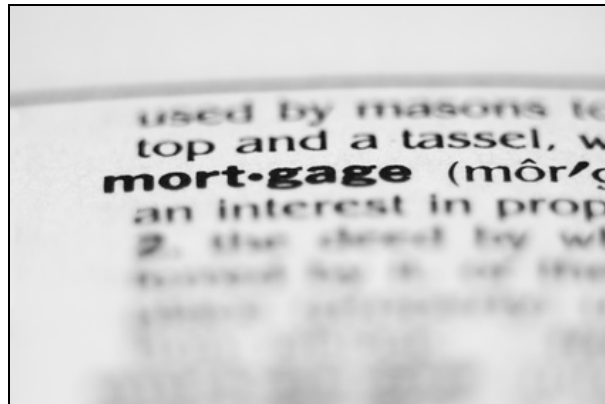


Financial Instruments

Overview

The objective of this project is to improve the usefulness of financial instrument reporting for users of financial statements and simplify the accounting requirements for financial instruments. The project will reconsider the recognition and measurement of financial instruments, address issues related to impairment of financial instruments and hedge accounting and increase convergence in accounting for financial instruments. Currently, the FASB and IASB have reached different conclusions on some key aspects of the project. The FASB issued an exposure draft on May 26, 2010, with the comment period ending September 30, 2010. The effective date has not been established, however, as proposed, nonpublic entities with less than \$1 billion in total assets will have an additional four years after the effective date for public entities to comply with certain requirements pertaining to loans, loan commitments and core deposit liabilities.

The FASB held a webcast to provide an overview of the proposed Accounting Standards Update on June 30, 2010. An archived version of the webcast and slides are available on the FASB website.



Scope

The standard would apply to financial instruments with certain exceptions. A financial instrument is cash, evidence of an ownership interest in an entity, or a contract that both: a) imposes on one entity a contractual obligation to either deliver cash or another financial instrument to a second entity or exchange other financial instruments on potentially unfavorable terms with the second entity **and** b) conveys to that second entity a contractual right either to receive cash or another financial instrument from the first entity or exchange other financial instruments on potentially favorable terms with the first entity.

There are a number of financial instruments excluded from the scope of this project including the following:

- Benefit plan obligations
- Insurance contracts
- Leased assets and liabilities
- Equity instruments classified as equity
- Interests in variable interest entities that the reporting entity consolidates
- Noncontrolling interests and equity investments in consolidated subsidiaries

The Impact to a Commercial Entity

Commercial entities for which financial instruments are limited to trade accounts receivable and payable as well as debt will likely not be impacted by this standard to a significant degree if these instruments meet the criteria to continue to be carried at amortized cost. Note however that convertible debt and/or debt with embedded derivatives requiring bifurcation under existing guidance will not be eligible to be carried at amortized cost under the proposed guidance.

Measurement and Classification

Initial Measurement – The FASB has designated a number of categories for this project including fair value, changes accounted for in net income: “FV-NI” and fair value, changes accounted for in other comprehensive income (a part of equity): “FV-OCI”. For FV-NI instruments, initial measurement would be at fair value with any difference between the transaction price and the fair value on the transaction date recorded immediately in net income. For FV-OCI instruments, initial measurement would be at transaction price. For financial instruments carried at amortized cost, initial measurement would be at the transaction price.

For core deposit liabilities of banks, initial measurement would be at the net present value of the average core deposit liability amount, discounted using the rate differential between the alternative funds rate and the all-in-cost-to-service rate over the implied maturity.

Subsequent Measurement – Except in the following circumstances, financial instruments would be subsequently measured at fair value with changes in fair value recognized in net income. Entities can choose to recognize certain changes in fair value through other comprehensive income if both of these conditions are met:

- The entity’s business strategy is to hold the debt instruments with principal amounts for collection or payment of the contractual cash flows, instead of selling or settling with a third party.
- The instrument has a stated maturity date, can’t be prepaid or settled in a way that the holder would not get substantially all of its initial investment, and is not a derivative, a hybrid containing a derivative, or an equity security.

An entity’s election that changes in fair value be recorded in OCI can only be made at initial recognition, and subsequent reclassification is prohibited.

Certain types of investments that can be redeemed with the issuer for only a specified amount such as stock in the Federal Home Loan Bank System and Federal Reserve Bank should be measured at redemption value.

Entities could also make an election to measure certain types of their own debt at amortized cost if the entity’s business strategy is to hold the liability for payment of contractual cash flows and if measuring the debt at FV would create or exacerbate a measurement attribute mismatch. The following criteria are deemed to create or exacerbate a measurement attribute mismatch:

- Liability contractually linked to an asset that is not measured at fair value
- Liability is associated with an operating segment for which less than 50 percent of recognized assets are subsequently measured at fair value
- Liability is of a consolidated entity for which less than 50 percent of consolidated recognized assets are subsequently measured at fair value

Hedge accounting changes would include elimination of the shortcut method and critical terms match method.

Core deposit liabilities would be remeasured each period using a current value method that reflects the economic benefit that an entity receives from this lower cost, stable funding source. Thus, the effects of changes in market interest rates would be transparent on core deposits.

These decisions would result in a rather significant increase in the number of situations requiring the use of fair value. Loans held for investment and nonmarketable equity securities, currently accounted for at amortized cost, would be measured at fair value.

Impairment

For FV-OCI assets, an entity must determine if a credit loss exists at the end of each reporting period. A credit impairment loss would be recognized when an event indicates the entity will not be able to collect all of the contractual cash flows for originated financial assets and amounts expected to be collected at

acquisition for purchased assets. An entity should not wait until a credit loss is probable to recognize a credit impairment.

For FV-OCI assets that are assessed for impairment on an individual basis, the FASB reached a decision that, even if the asset is not impaired based on the entity's assessment of the asset on an individual basis, a credit impairment still might be appropriate based on loss experience with financial assets with similar characteristics.

For credit impairments of pools of homogeneous assets for which impairment is assessed based on a historical loss rate, the FASB has decided that the amount of credit impairment to be recognized in net income should be determined by applying an aggregate loss rate to the pool balance in the period during which the assets were originated. In subsequent periods, any changes in the loss rate would generally result in recognizing additional impairment, or reversing previously recognized impairment losses.

Interest Income Recognition

Interest income on FV-OCI assets would be calculated using the carrying value of the loan (amortized cost less allowance of credit impairment). The net carrying value would be multiplied by the effective interest rate. Any cash received in excess of accrued interest would increase the allowance. Any difference between the amount of the accrued interest receivable based on the contractual interest due and the amount of interest based on applying the effective interest rate would increase the allowance.

Presentation

Based on the decisions to date, entities would be required to include one statement of financial performance with a total for comprehensive income (including a subtotal for net income) for each reporting period. Financial instruments would be presented separately on the statement of financial position based on whether they are FV-NI or FV-OCI.

FV-NI Financial Instruments – An entity would be required to present the fair value amount on the face of the statement of financial position (except for the entity's own debt, for which the entity would be required to present the amortized cost). An entity would be required to present an aggregate amount for realized and unrealized gains and losses on the face of the income statement.

For financial liabilities, an entity would also have to present on the face of the performance statement a significant current-period change in fair value attributable to the entity's credit standing.

FV-OCI Financial Instruments – An entity would be required to present as separate line items in the statement of financial position the amortized cost and the amount required to adjust amortized cost to arrive at fair value. For financial assets, an entity also would need to present a separate line item for allowance for credit losses. An entity would have to present separately on the face of the performance statement the current period interest income and expense accruals, credit losses, and realized gains or losses. For financial liabilities, an entity would also have to present on the face of the performance statement a significant current-period change in fair value attributable to the entity's credit standing.

Financial Instruments for Which the Amortized Cost Option Is Elected – For an entity's own debt for which the amortized cost option is elected, the entity would be required to present separately in the performance statement both the current period expense accruals (including amortization (accretion) of premium (discount) upon acquisition) and realized gains or losses.

Core Deposit Liabilities – Specific presentation requirements exist for core deposit liabilities and are dependent upon whether the entity presents changes in the remeasured amount in other comprehensive income or net income.

IASB/FASB Differences

The following presents a brief summary of the provisions of IFRS 9:

- An entity would recognize a financial asset at amortized cost if the business model is to hold the asset to collect the contractual cash flows and the cash flows are required on specified dates and are solely payments of principal and interest.
- If an entity changes its business model, the assets must be reclassified and accounted for prospectively in accordance with the revised business model.
- If an equity instrument is not held for trading, it can irrevocably be designated as FV-OCI.
- An entity would not separate a hybrid financial asset into a host and the embedded derivative. Instead, the entity would classify and account for the single instrument based on the business model and the terms of the financial asset.
- All other financial assets are accounted for as FV-NI.

Financial liabilities are not in the scope of IFRS 9 however the IASB has tentatively decided to retain existing guidance to record most financial liabilities at amortized cost.

Leases

Overview

This project's objective is to create common lease accounting requirements to ensure that the assets and liabilities arising from lease contracts are recognized in the statement of financial position. The lease project will result in significant changes to the model for lease accounting. The FASB issued an exposure draft on August 17, 2010, with a comment period ending December 15, 2010. The exposure draft did not specify a proposed effective date. The proposed approach is a "right-of-use" model. This approach will result in a significant change to current practice in that all leases would be reflected in some manner on the balance sheets of both the lessee and the lessor. Effectively, all leases would be treated as capital leases. Note that this is likely to significantly impact many company's financial ratios and covenants.

Scope

The standard would apply to all leases of property, plant and equipment. Some contracts specifically excluded from the scope include leases of intangible assets, leases related to minerals, oil, natural gas and similar non-regenerative resources, and leases of biological assets. Additionally, contracts that represent the purchase or sale of an asset are also excluded from the scope. A simplified recognition model for leases with maximum possible terms of less than one year (*i.e.*, recognize a lease asset and liability equal to the gross payments remaining on each lease) is included.



Lessee Accounting

Under the proposed model, lessees would recognize an asset for the right to use the leased asset, and a liability for the obligation to make rental payments. The liability would be recorded at "cost," which is defined as the present value of the rental payments discounted using the lessee's incremental borrowing rate or the rate that the lessor charges the lessee (if that can be determined). The asset would be recorded at that amount plus any initial direct costs. Subsequently, the asset and liability would be recorded at amortized cost.

With respect to the lease term, a lessee would include renewal options in the determination of the lease term if it is reasonably assured that the lessee will exercise the option(s). (Purchase options would be treated the same way.) The lease term is the longest possible term that is more likely than not to occur. A lessee would consider past practices and current intentions in looking at renewal and purchase options when determining the lease term.

Contingent cash flows would enter into the initial measurement of the obligation as opposed to the current model that recognizes them as expenses in the period in which they are incurred. The contingent cash flows would enter into the measurement using an "expected outcomes" approach.

Lessees will be required to reassess the carrying amount of the obligation each reporting period if facts or circumstances indicate that there would be a significant change in the liability. Lessees would recognize the effect of any changes in estimates arising from changes in the estimated lease term by adjusting the balance of the right-of-use asset. With respect to changes in estimates of contingent cash flows, if the changes arise from current or prior-period activities or events, the impact is recognized in income. The effects of all other changes are recognized by adjusting the lessee's right-of-use asset.

Lessor Accounting

The proposed model contains two approaches for lessor accounting—the performance obligation approach and the derecognition approach. Under either approach, a lessor would record an asset for the present value of the expected lease payments plus any recoverable initial direct costs. The accounting for the obligation will depend on whether the lessor retains exposure to significant risks or benefits related to the leased asset. If the lessor retains significant exposure to such risks, it would apply the performance obligation approach. If the lessor does not retain such risks, it would apply the derecognition approach.

Under the performance obligation approach, the lessor is considered to retain the underlying leased asset. Therefore, that asset is not taken off the books (derecognized). The lessor would record a liability representing the performance obligation. The liability would initially equal the lease receivable (less any initial direct costs incurred by the lessor).

Both the asset and the liability would be reduced in a systematic and rational manner based on the pattern of use of the underlying leased asset.

While the lessor's treatment of options would be the same as a lessee's (as discussed above), the lessor and lessee might have different estimates of the likelihood of exercise, so the two parties may not account for the options in identical fashions.

With respect to contingent cash flows, lessors would be required to recognize receivables for contingent rentals and residual value guarantees, but only if the amounts can be measured reliably.

The expected lease payments must be reassessed each reporting period if any new facts or circumstances indicate a significant change in estimates or judgments.

Any changes in a receivable arising from a change in estimated lease term will be recognized as a change in the performance obligation. If the change results from a change in estimated cash flows, the accounting would depend on whether the performance obligation had been satisfied. If the performance obligation had been satisfied, changes would be recognized in income. If it had not been satisfied, changes would be accounted for as changes to the carrying amount of the liability.

Under the derecognition approach, the lessor will remove a portion of the carrying amount of the underlying leased asset from its accounts, representing the lessee's right to use the underlying asset during the lease term. The amount of the asset retained by the lessor represents a residual portion for the lessor's rights in the underlying asset that did not transfer. This could result in income or loss being recognized by the lessor at lease inception.

The following table summarizes the current decisions on both lessee and lessor accounting:

	Lessee	Lessor
Recognition	Recognize an asset for right to use	Recognize a receivable
	Recognize a liability for obligation to make rental payments	<u>Performance obligation approach:</u> Recognize a liability for obligation to permit lessee to use leased asset
	Record at cost; equal to present value of rental payments, determined using the entity's incremental borrowing rate or the rate the lessor is charging the lessee (if that can be determined)	Record receivable using implicit rate <u>Derecognition approach:</u> Record a receivable Derecognize a portion of the asset
Subsequent measurement	Measured at amortized cost	Record receivable at amortized cost (resulting in interest income)
		<u>Performance obligation approach:</u> Performance obligation would decrease over lease term, in a systematic and rational fashion
Lease term/options	Renewal options included in lease term if it is reasonably assured that the lessees will exercise	Consider renewal options, but the likelihood assessment may differ from lessee's assessment
	Purchase options are accounted for only when they are exercised.	Purchase options are accounted for only when they are exercised.
	Lease term equals longest period that is "more likely than not" to be used.	
Contingent cash flows	Include in the obligation under an "expected outcome" estimation	Recognize in accounts receivable, if the receivable could be reliably measured
Changes in estimates	Lease term—reflected by revising right-to-use asset	Lease term—reflected by revising performance obligation
	Contingent cash flows—to income statement (for changes in current or prior periods) or to the right-to-use asset (for all other changes)	Contingent cash flows—to revenue if performance obligation has been satisfied; if not, adjust performance obligation

Financial Instruments with Characteristics of Equity

Overview

The objective of this project is to improve and simplify the financial reporting requirements for financial instruments with characteristics of equity. Current guidance on classification of financial instruments with characteristics of equity has accumulated through the issuance of more than 60 pronouncements over many years, and is often viewed as being difficult to understand. This project will: (a) eliminate the current guidance in the Codification on classification of financial instruments with characteristics of equity, and (b) provide investors with more useful information.

In 2007, the FASB issued a Preliminary Views document which described three possible approaches for distinguishing between equity and liabilities or assets. However, none of the approaches discussed in the Preliminary Views document will be pursued. Rather, International Accounting Standards (IAS) 32, *Financial Instruments: Presentation*, will be used as a basis for the standard. Using IAS 32 as a model, the FASB and IASB have proceeded to address the classification of particular instruments with identified practice issues. These decisions will then be used to develop a set of principles that produce the desired classification results.

Some of the decisions reached will result in a change from current practice under U.S. GAAP. Classification results under the proposed standard may be different than those under current U.S. standards. For example, preferred shares convertible into a variable number of common shares at the option of the holder often receive equity classification with no subsequent remeasurement under existing U.S. standards. However, under the proposed model, liability classification would be required, and the measurement guidance developed under the *Financial Instruments* project would apply.



Scope

The proposed requirements would apply to all financial instruments except: (a) interests in subsidiaries, associates, or joint ventures that are accounted for under other standards, (b) employers' rights and obligations under employee benefit plans, (c) insurance contracts accounted for under other standards, and (d) share-based payment awards.

Instruments Classified as Equity in their Entirety

The types of instruments that would be classified as equity in their entirety include perpetual instruments without specified limits to their lives, contracts that require or may require an entity to issue a specified number of its own perpetual equity instruments in exchange for a specified price (e.g., call options and forward contracts to issue shares), and preferred shares required to be converted into a specified number of common shares on a specified date or on the occurrence of an event that is certain to occur.

Classification of Convertible Debt

As currently proposed, convertible debt would be separated into a liability component and an equity component if it is convertible at the option of the holder into a specified number of instruments that will be equity in their entirety when issued. All other convertible debt instruments would be classified as liabilities in their entirety.

Assessment of an Entity's Ability to Settle in Shares

The entity's ability to issue shares to settle share-settled instruments classified as equity would be assessed at the date the instrument is issued and at each reporting date thereafter. If, at any time, the entity does not have enough authorized shares to settle the instrument, the instrument would be reclassified as a liability and would remain in that classification until settled.

Consolidation

Overview

The objective of this joint project is to provide comprehensive guidance for consolidation of all entities, including entities controlled by voting or similar interests. This project comes on the heels of the FASB's recent issuance of Statement No. 167 (Topic 810 of the Codification) to provide updated guidance on variable interest entities (the VIE standards) as well as the IASB's issuance of an exposure draft on consolidations in December 2008.

In this project, the basis for consolidation of another entity by a reporting entity will be control. A reporting entity will likely be considered to control another entity (and hence be required to consolidate that entity) when it has the power to direct the activities of that other entity and the ability to benefit from that power. The power to direct the activities of another entity exists if a reporting entity has the current ability to direct the activities of that entity that significantly affect its returns. When evaluating whether a reporting entity has this power, consideration would be given to substantive participating rights held by the reporting entity. For example, if the reporting entity has the right to step in and make substantive decisions at the only time they are required to be made, the reporting entity would be considered to have this power. A reporting entity must have some exposure to risks and rewards to benefit from its power to direct the activities of another entity and hence control that entity. The level of these risks and rewards would be an indicator of control.

Scope

All entities other than investment companies would be in the scope of the consolidation guidance, including both traditional "voting interest" entities and "variable interest" entities covered by the VIE standards. An investment company would measure investments in entities that it controls at fair value. However, the parent of an investment company (if it is not an investment company itself) is prohibited from retaining the fair value accounting applied by its investment company subsidiary and must consolidate all entities that it controls.

Basis for Determining Control

Control may be achieved through the contractual ability to direct the activities of another entity. This is often based on ownership of more than half of the voting rights in an entity controlled by voting rights. When assessing whether a reporting entity has control through voting rights, it should consider substantive options and convertible instruments of the other entity. In addition, contractual rights obtained through other arrangements that relate to substantial activities of the entity also would be considered when evaluating an entity's contractual ability to direct the activities of another entity.

Control also may be achieved in situations in which a reporting entity has the ability to direct the activities of another entity based on other-than-contractual arrangements. For instance, a reporting entity with less than half of the voting rights in another entity controlled by voting rights may still control that other entity. This control may be based on the reporting entity's existing voting rights that the entity believes give them the power to direct the activities of the other entity combined with the fact that other parties could not prevent the reporting entity from exerting this power. Indicators of this ability to direct could include the reporting entity's ability to obtain additional voting rights in the entity, the entity's operations being dependent on the reporting entity, or the size of the

reporting entity's voting rights being large relative to the size and dispersion of other vote holders along with historical voting patterns of the other vote holders being consistent with the reporting entity.

The control assessment must be evaluated continuously based on existing facts and circumstances. While the preceding will result in a different evaluation to determine whether a variable interest entity should be consolidated as compared to existing U.S. GAAP, the FASB expects that the ultimate conclusions will be the same.

Related Parties

When evaluating whether a reporting entity controls another entity, consideration must be given to related parties of the reporting entity. The involvement and interests of related parties would be considered to be those of the reporting entity when the nature of the reporting entity's related-party relationship is such that the related party is acting on behalf of the reporting entity. This would be the case when those that direct the activities of the reporting entity also have the ability to direct another entity to act on the reporting entity's behalf. It is expected that the final consolidation standard will include a list of potential related parties and guidance similar to that currently in ASC Topic 810 to address situations in which a reporting entity and its related parties as a group meet the control requirements.

Agency Relationships

The assessment of whether a decision maker is an agent or principal is necessary because a principal could be required to consolidate another entity if it controls that other entity. This determination (a) should be made based on the overall relationship between the decision-maker, the entity being managed and other interest holders and (b) should consider the following factors:

- Scope of decision-making authority;
- Rights held by other parties; and
- The decision maker's remuneration and exposure to variability of returns because of other interests that it holds in the entity.

Investment Companies

To be considered an investment company, an entity would need to meet all of the following criteria:

- Express business purpose is investing for current income, capital appreciation, or both;
- Potential exit strategies and an expected time to exit investments have been identified;
- Substantially all activities are for generating income, capital appreciation, or both;
- Ownership is represented by units of investments;
- The funds of the owners are pooled to avail them of professional investment management;
- All investments are managed and performance is evaluated on a fair value basis;
- Be a reporting entity; and
- Any debt providers to an entity's investees must not have direct recourse to the entity's other investees.

Fair Value Measurements

Overview

This joint project's objective is to create converged fair value measurement guidance. This project is intended to conform the meaning of the term "fair value" in U.S. GAAP and IFRSs, and ensure the fair value measurement and disclosure requirements under both sets of standards are the same (other than minor wording or style differences).

On June 28, 2010, the FASB issued an exposure draft of the proposed Accounting Standards Update (ASU), *Fair Value Measurements and Disclosures (Topic 820) - Amendments for Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. The proposed ASU includes both wording changes and clarifications of existing fair value measurement guidance, as well as amendments to some of the principles and requirements for measuring fair value and disclosing information about fair value.

Scope

The current scope of the U.S. GAAP fair value measurement guidance (ASC Topic 820) would not be changed.

Highest and Best Use

The exposure draft would establish that the "highest and best use" and "valuation premise" concepts are relevant only when measuring the fair value of nonfinancial assets. These concepts are not relevant when measuring the fair value of financial assets or of liabilities. A fair value measurement of a nonfinancial asset would consider the use of the assets that would provide maximum value (that is, the highest and best use) determined from the perspective of market participants.

The concept of "valuation premise" will be described without using the terms "in use" or "in exchange". The highest and best use of a nonfinancial asset establishes its valuation premise which may be on a standalone basis or through its use in combination with other assets as a group or in combination with other assets and liabilities.

Financial Instruments Managed Within a Portfolio

An exception to the fair value measurement requirements is provided in the exposure draft for financial instruments that are managed within a portfolio. Reporting entities that hold financial assets and financial liabilities often manage those instruments on the basis of the reporting entity's net, rather than gross, exposure to a particular market risk or to the credit risk of a particular counterparty. When the reporting entity manages that group of financial assets and financial liabilities on the basis of its net exposure to either of those risks, the reporting entity is permitted to measure the fair value of the group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk or to transfer a net short position (that is, a liability) for a particular risk in an orderly transaction between market participants at the measurement date. A number of conditions must be met to utilize this exception.

Instruments Classified in Shareholders' Equity

The exposure draft requires that instruments classified in shareholders' equity, such as equity interests issued as consideration in a business combination, a reporting entity would measure the fair value of its own equity instrument from the perspective of a market participant who holds the instrument as an asset.

Blockage Factors and Other Premiums and Discounts

A blockage factor represents the concept that a reduction from a quoted market price is necessary to reflect that a large block of shares may sell for less than what an individual share would. Blockage factors would be prohibited at any level of the fair value hierarchy (as opposed to current U.S. GAAP which prohibits them at Level 1). However, other premiums and discounts (for example, a control premium or a noncontrolling interest discount) would be taken into account if market participants would consider those premiums or discounts when pricing an asset or a liability given the unit of account.

Additional Disclosures

The exposure draft expands fair value measurement disclosures to include information about the measurement uncertainty inherent in fair value measurements categorized within Level 3 of the fair value hierarchy. A reporting entity would be required to disclose the effect on a fair value measurement of changing one or more unobservable inputs that could have reasonably been used to measure fair value in the circumstances.

About McGladrey & Pullen, LLP

McGladrey is the brand under which McGladrey & Pullen, LLP and RSM McGladrey, Inc. serve clients' business needs. The two firms operate as separate legal entities in an alternative practice structure. McGladrey & Pullen is a licensed CPA firm providing assurance services. RSM McGladrey provides tax and consulting services.

McGladrey & Pullen, LLP and RSM McGladrey, Inc. are members of the RSM International ("RSMi") network of independent accounting, tax and consulting firms. The member firms of RSMi collaborate to provide services to global clients, but are separate and distinct legal entities which cannot obligate each other. Each member firm is responsible only for its own acts and omissions, and not those of any other party.

McGladrey, the McGladrey signature, The McGladrey Classic logo, *The power of being understood*, *Power comes from being understood* and *Experience the power of being understood* are trademarks of McGladrey & Pullen, LLP and RSM McGladrey, Inc.

Appendix A – Examples from the FASB’s Staff Draft of an Exposure Draft on Financial Statement Presentation

STATEMENT OF COMPREHENSIVE INCOME

	For the Years Ended	
	December 31,	
	20X1	20X0
BUSINESS		
Operating		
Revenue	3,487,600	3,239,250
Cost of goods sold	(1,956,629)	(1,816,903)
Gross profit	1,530,971	1,422,347
Selling expenses	(153,268)	(130,034)
General and administrative expenses	(469,754)	(433,950)
Other operating income (expense)	17,663	(2,025)
Impairment loss on goodwill	-	(35,033)
Operating income before operating finance costs	925,612	821,305
Operating finance costs	(33,235)	(33,250)
Total operating income	892,377	788,055
Investing		
Dividend and interest income	62,619	55,500
Earnings in Company A (equity method)	23,760	22,000
Realized gain on securities	18,250	7,500
Fair value change in investment in Company B	7,500	3,250
Total investing income	112,129	88,250
TOTAL BUSINESS INCOME	1,004,506	876,305
FINANCING		
Debt		
Interest expense	(111,352)	(110,250)
TOTAL FINANCING EXPENSE	(111,352)	(110,250)
Income from continuing operations before taxes	893,154	766,055
INCOME TAX		
Total income tax expense	(333,625)	(295,266)
Income from continuing operations	559,529	470,789
DISCONTINUED OPERATION		
Loss on discontinued operation	(32,400)	(35,000)
Income tax benefit	11,340	12,250
NET LOSS ON DISCONTINUED OPERATION	(21,060)	(22,750)
NET INCOME	538,469	448,039
OTHER COMPREHENSIVE INCOME (net of tax)		
Gains on available-for-sale securities arising during the year	29,056	20,150
Amounts reclassified into earnings	(11,863)	(4,875)
Unrealized gain on securities (investing)	17,193	15,275
Gains on futures contracts arising during the year	3,784	3,503
Amounts reclassified into earnings	(1,959)	(1,813)
Unrealized gain on futures contracts (operating)	1,825	1,690
Foreign currency translation adjustment on equity method investee (investing)	(1,404)	(1,300)
	2,094	(1,492)
TOTAL OTHER COMPREHENSIVE INCOME	19,708	14,173
TOTAL COMPREHENSIVE INCOME	558,177	462,212
Net income per share—basic	7.07	6.14
Net income per share—diluted	6.85	5.90

STATEMENT OF FINANCIAL POSITION

	As of December 31,	
	20X1	20X0
BUSINESS		
Operating		
Cash (see Note 6)	74,102	61,941
Accounts receivable, trade (net of allowance)	922,036	527,841
Inventory	679,474	767,102
Prepaid advertising and other	86,552	78,150
Total short-term operating assets	1,762,164	1,435,034
Property, plant, and equipment (net of accumulated depreciation)	2,838,660	3,064,200
Goodwill and other intangible assets	189,967	189,967
Total long-term operating assets	3,028,627	3,254,167
Advances from customers	(182,000)	(425,000)
Accounts payable, trade	(612,556)	(505,000)
Wages, salaries, and benefits payable, and share-based compensation liability	(212,586)	(221,165)
Total short-term operating liabilities	(1,007,142)	(1,151,165)
Total long-term liabilities	(3,848)	(1,850)
Net operating assets before operating finance	3,779,801	3,536,186
Operating finance		
Short-term portion of lease liability and interest payable on lease liability (see Note 6)	(50,000)	(50,000)
Total short-term operating finance liabilities	(50,000)	(50,000)
Accrued pension liability	(293,250)	(529,500)
Long-term portion of lease liability (see Note 6)	(261,325)	(296,500)
Decommissioning liability	(29,640)	(14,250)
Total long-term operating finance liabilities	(584,215)	(840,250)
Total operating finance liabilities	(634,215)	(890,250)
Net operating assets	3,145,586	2,645,936
Investing		
Short-term investments (see Note 6)	1,100,000	800,000
Available-for-sale securities (see Note 6)	473,600	485,000
Total short-term investing assets	1,573,600	1,285,000
Equity method investment in Company A	261,600	240,000
Investment in Company B at fair value	46,750	39,250
Total long-term investing assets	308,350	279,250
Total investing assets	1,881,950	1,564,250
NET BUSINESS ASSETS	5,027,536	4,210,186

STATEMENT OF FINANCIAL POSITION (continued)

	As of December 31,	
	20X1	20X0
FINANCING		
Debt		
Short-term debt and interest payable (see Note 6)	(702,401)	(512,563)
Dividends payable	(20,000)	(20,000)
Total short-term debt	(722,401)	(532,563)
Total long-term debt (see Note 6)	(2,050,000)	(2,050,000)
Total debt	(2,772,401)	(2,582,563)
Equity		
Common stock (par .01, 100,000 shares authorized and issued both years; 76,149 and 73,000 shares outstanding December 31, 20X1 and 20X0, respectively)	(761)	(730)
Additional paid-in capital	(1,514,839)	(1,506,770)
Treasury stock	88,360	164,500
Retained earnings	(1,100,358)	(648,289)
Accumulated other comprehensive income	(158,081)	(138,373)
Total equity	(2,685,679)	(2,129,662)
TOTAL FINANCING	(5,458,080)	(4,712,225)
INCOME TAX		
Income taxes payable	(72,514)	(63,678)
Deferred tax asset	46,226	89,067
NET INCOME TAX (LIABILITY) ASSET	(26,288)	25,389
DISCONTINUED OPERATION		
Assets of discontinued operation	856,832	876,650
Liabilities of discontinued operation	(400,000)	(400,000)
NET ASSETS OF DISCONTINUED OPERATION	456,832	476,650
Total short-term assets	4,192,596	3,596,684
Total long-term assets	3,383,203	3,622,484
TOTAL ASSETS	7,575,799	7,219,168
Total short-term liabilities	(2,252,057)	(2,197,406)
Total long-term liabilities	(2,638,063)	(2,892,100)
TOTAL LIABILITIES	(4,890,120)	(5,089,506)

Appendix B - Financial Accounting Standards Board

Current Technical Plan of Selected Projects* (as of August 27, 2010)

	2010		2011			
	3Q	4Q	1Q	2Q	3Q	4Q
Fair Value Measurement (<i>Exposure Draft issued 06/29/10. Updated August 26, 2010</i>)	C		F			
Consolidation: Policy and Procedures						
Voting Interest Entities (<i>Updated August 10, 2010</i>)		R				
Investment Companies (<i>Updated August 10, 2010</i>)		E		F		
Accounting for Financial Instruments (<i>Exposure Draft issued 05/26/10. Updated August 5, 2010</i>)	C	R		F		
Financial Instruments with Characteristics of Equity (<i>Updated July 15, 2010</i>)			E		R	F
Financial Statement Presentation (<i>Staff Draft issued 07/01/10. Updated August 3, 2010</i>)			E		R	F
Insurance Contracts (<i>Updated August 2, 2010</i>)	D					
Leases (<i>Exposure Draft issued 08/17/10. Updated August 17, 2010</i>)		C,R		F		
Revenue Recognition (<i>Exposure Draft issued 06/24/10. Updated August 17, 2010</i>)		C,R		F		
Statement of Comprehensive Income (<i>Exposure Draft issued 05/26/10. Updated June 1, 2010</i>)	C	F				
Reporting Discontinued Operations (<i>Updated July 29, 2010</i>)			E			F
Balance Sheet—Offsetting (<i>Updated June 21, 2010</i>)		E	R	F		
Disclosure of Certain Loss Contingencies (<i>Exposure Draft issued 07/20/10. Updated August 27, 2010</i>)	C	F				
Going Concern (<i>Updated April 13, 2010</i>)		E	F			
Disclosures about an Employer's Participation in a Multiemployer Plan (<i>Updated April 19, 2010</i>)	E	F				
Investment Properties (<i>Updated July 23, 2010</i>)	E			F		

* Information about all FASB and EITF projects is available at www.fasb.org

Codes:

- C – Comment Deadline
- D – Discussion Paper
- E – Exposure Draft
- F – Final Document
- R – Roundtable Discussion