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## Subsequent Events: New Standards Apply

The Financial Accounting Standards Board (FASB) launched the *Accounting Standards Codification* on July 1, 2009. The objective of the Codification is to be the single authoritative source of U.S. generally accepted accounting principles. The Codification, which was effective for periods ending after September 15, 2009, supersedes all other sources of U.S. GAAP. The only guidance in professional standards on subsequent events was contained in the auditing literature, specifically AU 560, *Subsequent Events*. The FASB wanted to make the accounting standards complete and undertook a project to bring the subsequent events guidance into the accounting standards. A similar project was started related to going concern guidance. That project has not been completed yet.

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## How Have the Standards Changed?

The FASB issued Statement of Accounting Standards No. 165, *Subsequent Events*, in May 2009. It is now included in the Codification in Topic 855. Some aspects of Statement 165 were not controversial and did not change practice. Other parts caused concern and were addressed with an amendment in February 2010 with Accounting Standards Update ("ASU", the new format to issue standards) No. 2010-09, *Subsequent Events, Amendments to Certain Recognition and Disclosure Requirements*<sup>1</sup>.

### New Terminology

One part of the Standards that is not confusing or controversial and is not a change from the prior guidance is when to recognize an event that happens after the balance sheet date:

New Terminology	Old Terminology (From AU 560)	Description
Recognized Subsequent Events	"Type 1"	Events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements
Nonrecognized Subsequent Events	"Type 2"	Events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date

The Standard requires the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements, to be recognized in the financial statements.

Subsequent events that provide evidence about conditions that did *not* exist at the date of the balance sheet but arose after the balance sheet date but before financial statements are issued or are available to be issued are not recognized, but should be considered for disclosure.

### New Terms and Concepts

A part of the Standard that has caused some confusion relates to the length of the subsequent events period. The Standard introduces new concepts and descriptions that are essential to understanding when the subsequent event period stops:

New Terminology	Description
Financial statements are issued	Financial statements are considered issued when they are widely distributed to shareholders and other financial statement users for general use and reliance in a form and format that complies with GAAP.
Financial statements are available to be issued	Financial statements are considered available to be issued when they are complete in a form and format that complies with GAAP and all approvals necessary for issuance have been obtained, for example, from management, the board of directors, and/or significant shareholders. The process involved in creating and distributing the financial statements will vary depending on an entity's management and corporate governance structure as well as statutory and regulatory requirements.

<sup>1</sup> The effective date of the ASU was upon issuance: February 25, 2010, except for the use of issued date by conduit bond obligors. That portion of the amendment is effective for periods ending after June 15, 2010.

New Terminology	Description
Securities and Exchange Commission (SEC) Filer	<p>An entity that is required to file or furnish its financial statements with either of the following:</p> <ul style="list-style-type: none"> <li>• The Securities and Exchange Commission (SEC)</li> <li>• With respect to an entity (banks and savings associations) subject to Section 12(i) of the Securities Exchange Act of 1934, as amended, the appropriate agency under that Section</li> </ul> <p>Accordingly, companies filing or furnishing reports to the SEC or a Financial Institution Regulatory Authority under the 1933, 1934, and 1940 Acts are SEC filers.</p> <p>Entities that are not otherwise SEC filers whose financial statements are included in a submission by another SEC filer (for example under Section 3.05 of Regulation S-X) are not included within this definition.</p>
Conduit Bond Obligor	<p>Conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).</p> <p><i>Background:</i></p> <p>Some state or units of local governments or agencies are permitted to issue a conduit debt security (commonly referred to as municipal bonds or industrial revenue bonds). A conduit debt security is an offering by a governmental entity that is not for its own use but for the use of a private party (conduit bond obligor). Often the obligor is a not-for-profit entity, for example, hospitals, museums, and libraries. Some for-profit entities for which the security is issued in the form of an industrial revenue or development bond for a specific purpose are allowable by the Internal Revenue Code. In some instances, these conduit debt securities are traded in a public market (a domestic or foreign stock exchange or on an over-the-counter market, including local or regional markets).</p> <p>The conduit bond obligor is required to make or fund all interest and principal payments as they become due, and any future financial reporting requirements also are the responsibility of that conduit bond obligor.</p>
Revised Financial Statements	<p>Financial statements revised only for either of the following conditions:</p> <ul style="list-style-type: none"> <li>• Correction of an error (also referred to as a restatement)</li> <li>• Retrospective application of U.S. GAAP</li> </ul> <p>Revised financial statements are also considered to be reissued financial statements.</p>
Reissued Financial Statements	<p>An entity may need to reissue financial statements, for example, in reports filed with the SEC or other regulatory agencies. After the original issuance of the financial statements, events or transactions may have occurred that require disclosure in the reissued financial statements to keep them from being misleading. An entity shall not recognize events occurring between the time the financial statements were issued or were available to be issued and the time the financial statements were reissued unless the adjustment is required by GAAP or regulatory requirements. Similarly, an entity shall not recognize events or transactions occurring after the financial statements were issued or were available to be issued in financial statements that are later reissued in comparative form along with financial statements of subsequent periods unless the adjustment is required by GAAP or regulatory requirements.</p>

## What Is Required?

The table below highlights the requirements for evaluating subsequent events and disclosures in a variety of circumstances:

Circumstance	Evaluate Subsequent Events Through	Disclose the Date that Subsequent Events Have Been Evaluated Through? <sup>2</sup>
Entity is an SEC Filer	Date financial statements are issued (the filing date)	No
Entity is a conduit bond obligor and the bonds trade in a public market	Date financial statements are issued <sup>3</sup>	Yes, and also disclose that the date disclosed was the date the financial statements were <i>issued</i> .
Entity is not an SEC Filer and not a conduit bond obligor (i.e. all other entities)	Date financial statements are available to be issued	Yes, and also disclose that the date disclosed was the date the financial statements were <i>available</i> to be issued.
Revised financial statements are reissued: SEC Filer	Date financial statements are reissued, but for disclosure only purposes for the period from the original issuance date to the reissuance date <sup>4</sup>	No
Revised financial statements are reissued: conduit bond obligor	Date financial statements are reissued, but for disclosure only purposes for the period from the original issuance date to the reissuance date <sup>4</sup>	Yes. Both the originally issued date and the revised date.
Revised financial statements are reissued: all other entities	Date financial statements are reissued, but for disclosure only purposes for the period from the original available to be issued date to the reissuance date <sup>4</sup>	Yes. Both the originally available to be issued date and the revised date.
Reissued financial statements (all situations other than when the financial statements have been revised)	Date financial statements are reissued, but for disclosure only purposes for the period from the original issuance or available to be issued date to the reissuance date <sup>4</sup>	No for SEC filers. Yes for all other entities, but only the date through which subsequent events were originally evaluated. <sup>5</sup>

<sup>2</sup> This column reflects the changes resulting from the issuance of ASU 2010-09.

<sup>3</sup> Some conduit bond obligors file financial information on the Electronic Municipal Market Access (EMMA) website. EMMA was established to increase the broad comprehensive access to information in the municipal securities market. Other conduit bond obligors do not file information on EMMA. The FASB decided to not provide guidance on what constitutes "issuance date" in these circumstances and judgment will be necessary to decide when the financial statements are issued.

<sup>4</sup> After the original issuance of the financial statements, events or transactions may have occurred that require disclosure in the reissued financial statements to keep them from being misleading. Events occurring between the time the financial statements were issued or available to be issued and the time the financial statements were reissued should not be adjusted for, unless the adjustment is required by GAAP or regulatory requirements. If information is discovered that was available at the time the financial statements were originally issued or available to be issued that would have caused an adjustment had it been known, that information should be evaluated as to whether it is an indication that the previously issued statement contained a misstatement.

<sup>5</sup> If additional disclosures are made about events that occurred after the original issuance or available to be issued date, it would usually be necessary to disclose the date of such events.

## Other Disclosures

FAS 165 carried over a disclosure principle from the auditing standards:

Some nonrecognized subsequent events may be of such a nature that they must be disclosed to keep the financial statements from being misleading. For such events, an entity shall disclose the following:

- a. The nature of the event
- b. An estimate of its financial effect or a statement that such an estimate cannot be made.

An entity also shall consider supplementing the historical financial statements with pro forma financial data. Occasionally, a nonrecognized subsequent event may be so significant that disclosure can best be made by means of pro forma financial data. Such data shall give effect to the event as if it had occurred on the balance sheet date. In some situations, an entity also shall consider presenting pro forma statements, usually a balance sheet only, in columnar form on the face of the historical statements.



## Have the Audit Standards Changed?

Statement 165 does not change the auditor's responsibilities under AU 560, which requires the auditor to perform subsequent event procedures through the audit report date. Because the auditor's report should not be dated earlier than the date on which the auditor has obtained sufficient appropriate audit evidence to support the opinion, the auditor's report date can never be earlier than the date through which management has evaluated subsequent events. Because the auditor is concerned with events occurring through the date of his or her report that may require adjustment to, or disclosure in, the financial statements, the specific management representations relating to information concerning subsequent events should be made as of the date of the auditor's report. In order to coordinate these dates (such that the date through which management has evaluated subsequent events, the date of the management representation letter, and the date of the auditor's report are the same), the auditor may want to discuss these subsequent event requirements (including dating of the note if required) with management in advance of beginning the audit.

## Examples, Please!

FAS 165 provides the following examples of *recognized* subsequent events:

- If the events that gave rise to litigation had taken place before the balance sheet date and that litigation is settled, after the balance sheet date but before the financial statements are issued or are available to be issued, for an amount different from the liability recorded in the accounts, then the settlement amount should be considered in estimating the amount of liability recognized in the financial statements at the balance sheet date.
- Subsequent events affecting the realization of assets, such as receivables and inventories or the settlement of estimated liabilities, should be recognized in the financial statements when those events represent the culmination of conditions that existed over a relatively long period of time. For example, a loss on an uncollectible trade account receivable as a result of a customer's deteriorating financial condition leading to bankruptcy after the balance sheet date but before the financial statements are issued or are available to be issued ordinarily will be indicative of conditions existing at the balance sheet date. Thus, the effects of the customer's bankruptcy filing shall be considered in determining the amount of uncollectible trade accounts receivable recognized in the financial statements at the balance sheet date.

FAS 165 provides the following examples of *nonrecognized* subsequent events:

- Sale of a bond or capital stock issued after the balance sheet date but before financial statements are issued or are available to be issued
- A business combination that occurs after the balance sheet date but before financial statements are issued or are available to be issued, although FASB Codification Topic 805 (originally issued as Statement No. 141 [revised 2007], *Business Combinations*) requires specific disclosures in such cases.
- Settlement of litigation when the event giving rise to the claim took place after the balance sheet date but before financial statements are issued or are available to be issued
- Loss of plant or inventories as a result of fire or natural disaster that occurred after the balance sheet date but before financial statements are issued or are available to be issued
- Losses on receivables resulting from conditions (such as a customer's major casualty) arising after the balance sheet date but before financial statements are issued or are available to be issued
- Changes in the fair value of assets or liabilities (financial or nonfinancial) or foreign exchange rates after the balance sheet date but before financial statements are issued or are available to be issued
- Entering into significant commitments or contingent liabilities, for example, by issuing significant guarantees after the balance sheet date but before financial statements are issued or are available to be issued

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## Questions and Answers

### ***Question 1: Can you provide a sample disclosure for a non-SEC filer?***

A sample footnote is:

"These financial statements considered subsequent events through March 22, 2010, the date the financial statements were available to be issued."

### ***Question 2: May a non-SEC filer rely on the date of the auditor's report to communicate the date that subsequent events are evaluated through?***

No. The date through which subsequent events were evaluated must be disclosed in a footnote. It is also not acceptable to only reference "through the date of the auditor's report".

### ***Question 3: Should an SEC filer disclose that subsequent events have been considered through the filing date?***

Such disclosure is not required and should be discouraged for logistical reasons, however, management is not precluded from disclosing it.

### ***Question 4: A non-SEC filer concluded its 2009 financial statements were available to be issued on March 22, 2010. In June, it was acquired by a public company. The non public company financial statements will now be filed with the SEC in a registration statement on Form S-4 and a Form 8-K. What date should subsequent events be evaluated through?***

The non-SEC filer should evaluate subsequent events through March 22, 2010, the date the financial statements were originally available to be issued.

However, the auditor will need to perform appropriate procedures to satisfy the requirements of AU 550 (*Other Information in Documents Containing Audited Financial Statements*) and AU 711 (*Filings Under Federal Securities Statutes*) to allow the auditor's report to be included in a filing. These additional procedures would not change the date of the auditor's report.

### ***Question 5: If a non-SEC filer prints and distributes additional financial statements subsequent to the initial distribution, is this a reissuance? If the audit firm originally printed the financial statements and is requested to "print" additional copies of such statements, is this a reissuance?***

No. However, management may want to consider the length of time since the date the financial statements were originally available to be issued, significant events occurring subsequent to that date that they are aware of, and the company's current financial condition in relationship to other information that would be provided to financial statement users and whether it would be appropriate to communicate material events that have occurred subsequent to the date the financial statements were available to be issued in some fashion, such as through a transmittal letter.

The auditor would likely evaluate the reasons for the request and knowledge they have about subsequent events, as well as management's plans for communicating those events.

***Question 6: If it has been determined that additional subsequent events need disclosure in connection with a "revised" financial statement, how detailed does the disclosure need to be?***

The extent of the disclosure will depend on how complex the subsequent event is. In some situations, a very brief description may be appropriate, such as the dismissal of a significant lawsuit previously disclosed in the financial statements that had no accrual associated with it. Other situations, such as noncompliance with debt covenants that arose after the date the financial statements were originally issued or available to be issued where no waivers have been obtained and the lender now has the right to call the loan, may require more extensive disclosures. As described in footnote 4 of this document, subsequent events occurring after the original date the financial statements were issued or available to be issued generally are not recognized, however such non recognized subsequent events should be evaluated for disclosure.

***Question 7: If an error in previously issued financial statements is discovered in connection with a reissuance of those financial statements, should the previously issued financial statements be revised to correct the error?***

If the error is material, the previously issued financial statements should be revised.

***Question 8: If it has been determined that no additional subsequent events require disclosure in connection with a "revised" financial statement, does that fact need to be disclosed?***

A non-SEC filer will need to disclose the date through which subsequent events have been evaluated in the revised financial statements, but there is no requirement to disclose that no events have occurred since the original issuance.

***Question 9: Through what date does a bank that files a Form 10-K or Form 10-Q with its regulator need to evaluate subsequent events? Does that date need to be disclosed?***

Banks and savings associations that file forms with their regulator that are the equivalent of what they would file with the SEC are considered SEC filers. Therefore, subsequent events must be evaluated through the filing date, but the date does not need to be disclosed. Call reports would not meet these criteria.

***Question 10: Does a broker dealer follow the guidance for an SEC filer?***

Yes. A broker dealer is an SEC filer and must evaluate subsequent events through the filing date, but the date does not need to be disclosed.

***Question 11: Would an entity "going public" in an IPO be an SEC filer?***

No. In a voluntary initial registration statement an entity does not have an obligation to file with the SEC until after the registration statement is declared effective, or automatically goes effective in connection with a Form 10 registration. Accordingly, until an entity's registration is effective, the entity is considered a non-SEC filer, and should evaluate subsequent events through the date the financial statements are available to be issued and disclose such date. Once the registration is effective, in subsequent filings with the SEC, the entity will need to evaluate subsequent events through the date of the filing with the SEC, but will not need to disclose the date.

***Question 12: Does an entity that files financial statements with the Commodities Futures Trading Commission (CFTC) qualify as an SEC filer?***

No. An entity that files financial statements with the CFTC is not an SEC filer.