

# *The quarter close*

## A look at this quarter's financial reporting issues

*December 12, 2011*

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## *What you need to know—Q4—2011*

Welcome to the fourth quarter 2011 edition of *The quarter close*. As we approach the year-end reporting season, we have a little something for everyone. What's on your wish list? Whether it's the new goodwill impairment standard or the latest from the SEC on IFRS, we'll help you check that list twice. Here's a preview of what's inside:

**Front and center.** The European debt crisis, a busy FASB and IASB convergence agenda, proposals for mandatory auditor rotation, SEC views on moving to IFRS, the emerging debate on private company standard setting...there's no shortage of newsworthy topics this quarter. All of these topics—and more—got air time at the recent AICPA National Conference on Current SEC and PCAOB Developments, so our highlights of the conference kick-off this edition.

**Accounting hot topics.** We revisit some perennial favorites this quarter. Impairment assessments, pension accounting, revenue recognition, tax disclosures...let's just call them the "gifts that keep on giving." We've sprinkled in some recent "words of wisdom" from the regulators in Washington—so don't pass this section by.

**Hot off the press.** The FASB issued final guidance on goodwill impairment and delivered on several proposals, including the revised revenue recognition exposure draft and a trio of proposals on consolidation and investment-related topics. And, an important development on other comprehensive income: the FASB has agreed to defer one controversial element of the new standard.

**And lots more.** There are more goodies inside, including the latest on the leases and financial instruments projects, new disclosure guidance from the SEC, and an update on proxy access.

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## *Front and center*

### **Highlights from the AICPA conference**

The 2011 AICPA National Conference on Current SEC and PCAOB Developments (AICPA conference) was held last week in Washington, D.C. Always highly anticipated, this year's annual event didn't disappoint. Representatives from the SEC, PCAOB, FASB, and IASB all shared insights on various current topics, and even dropped some clues about areas that may warrant some extra attention during the year-end reporting season.

Make sure you check out our upcoming Dataline on the AICPA conference—due later this week—before heading out on holiday break. It will include PwC's thoughts on a number of matters discussed at the conference. Are you the type who can't help sneaking a peek? If so, we've summarized below a few of the themes and highlights to tide you over.

#### *The final say on IFRS? Not quite yet...*

We'll need to wait at least a few more months. That's how much time the SEC says it needs to complete its final report on its IFRS work plan and put itself in a position to determine the future of IFRS for U.S. public companies. The standard setters also weighed in on this topic. Both FASB Chairman Leslie Seidman and IASB Chairman Hans Hoogervorst seemed to generally support an endorsement approach (similar to the approach outlined by the SEC in its May 2011 paper), but with some nuances. Read more in "IFRS developments."

*I believe that the passage of a grain of sand in the hour glass of time is not nearly as critical as ensuring that we take this opportunity to establish a strong and lasting framework.*

-James L. Kroeker, SEC Chief Accountant, commenting on the SEC's IFRS work plan, [December 5, 2011](#)

### *We have to stop meeting like this...the future of convergence*

Look for the boards to work diligently to finish their priority projects in 2012. After that, however, the boards signaled that it's time for a new phase of standard setting. In other words, they don't view the current convergence process as a long-term solution. Exactly what will the future of standard setting look like? That may depend on the SEC's decisions about the path forward on incorporating IFRS.

### *Once again, it's the economy*

The challenging economic environment, including the ongoing European debt crisis, was a recurring theme throughout the conference. Some areas of focus: income taxes, goodwill impairment assessments, and pension plans (among others). We touch on each of these topics later in this publication. Not surprisingly, the SEC also highlighted the need for enhanced disclosures about exposures to the sovereign debt of several European countries.

### *The price is right...or is it?*

One topic was on virtually everyone's list: evaluating the use of pricing services to value investments. It was clear that the use of pricing services and management's responsibilities in this area—including disclosures and internal controls—are receiving more focus from the SEC. Additionally, the PCAOB has convened a task force on this topic. On the subject of valuation, the SEC also planted a seed about the need to add more structure to the valuation profession<sup>1</sup>. Expect to hear more on these matters in the upcoming year.

### *SEC dishes out traditional advice*

Segment reporting, loss contingencies, non-GAAP measures...sound familiar? These may seem like the "ghosts of AICPA conferences past," but there's good reason for the SEC to keep emphasizing the key messages in these areas. More details to come in our AICPA conference Dataline.

### *Everybody's talking about it—PCAOB puts the focus on auditing*

Auditing was a frequent topic of conversation...and it wasn't just the PCAOB. Many speakers took the opportunity to give their "two cents" on the PCAOB's recent concept releases, especially the possibility of term limits for audit firms. For an update on the PCAOB's activity, head to "On the horizon."

## **Private company standard-setting debate heats up**

In October, the Financial Accounting Foundation (FAF), the organization that oversees the FASB, issued its eagerly-awaited [proposal](#) on private company standard setting. Did it bring glad tidings? The FAF's proposal did incorporate many of the Blue-Ribbon Panel's<sup>2</sup> recommendations. However, the FAF did not embrace the Panel's recommendation to create an entirely separate standard setter for private companies.

Instead, the FAF proposed creating a Private Company Standards Improvement Council (the Council), an advisory group with similarities to the Emerging Issues Task Force

<sup>1</sup> Refer to SEC Deputy Chief Accountant Paul Beswick's speech. Beswick was unable to attend the AICPA conference, but his prepared remarks are available on the SEC's [website](#).

<sup>2</sup> In December 2009, the FAF created the Blue-Ribbon Panel on Standard Setting for Private Companies, sponsored jointly with the AICPA and the National Association of State Boards of Accountancy, to address how accounting standards can best meet the needs of U.S. users of private company financial statements.

***Underlying this recommendation is the FAF's belief that over time, the standards of two entirely separate boards will inevitably diverge, despite their best intentions. Hans [Hoogervorst, IASB Chairman] and I lead two boards with a serious desire to reach the same conclusions, and yet we do not always agree.***

- Leslie F. Seidman, FASB  
Chairman, [December 6, 2011](#)

(EITF). The Council would debate the merits of and make recommendations to adjust the requirements of U.S. GAAP for private companies. The Council's proposed changes would require ratification by the FASB and changes would be subject to public comment prior to a final FASB vote.

Why the big debate and who should care? Well, the impact extends beyond private companies—a point emphasized by FASB Chairman Leslie Seidman at last week's AICPA conference. A central element of the debate relates to complexity, which is a concern shared by both private and public companies. The FAF believes the FASB should address complexity and cost-benefit concerns more broadly, as these issues affect all constituencies. This was evident in recent standard-setting efforts, including the project on goodwill impairment.

The comment period for the FAF's proposal ends January 14. The FAF will also hold three roundtables early in 2012 to discuss the proposal. For a summary of its key components, see [In brief 2011-41](#), *Financial Accounting Foundation lays out its plan to improve standard setting for private companies*. You also might be interested in our recent point of view documents on complexity and private company standard setting: [Point of view](#), *Reducing complexity—Our proposal to address this challenge*, and [Point of view](#), *Setting private company accounting standards*.

#### *FASB continues outreach to private companies*

Meanwhile, other FASB initiatives in this area roll on. The FASB held two roundtables in October to get feedback from private companies and other stakeholders on existing standards. And, you may recall that the FASB began work earlier this year on a separate “decision-making framework” for private companies. A discussion paper is still expected on this framework, but the timing has been delayed, pending the outcome of the FAF's proposal.

This quarter, the FASB added to its agenda three new projects focused on nonpublic entities. First, the FASB agreed to consider exempting nonpublic entities from providing some of the required disclosures about “Level 3” fair value measurements. The FASB also added two projects with a goal of improving financial reporting of not-for-profit organizations, stemming from recommendations from the FASB's Not-for-Profit Advisory Committee. Stay tuned for more on these projects in 2012.

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## ***Accounting hot topics***

Does it seem like the same hot topics get pulled out each year like your neighbor's tacky holiday decorations? Yeah, we think so too...but we also know that you can't go into year end on autopilot. It's a good idea to revisit these issues since a company's circumstances may have changed since last year, not to mention the broader economic and regulatory environment. On that note, here are our year-end reminders.

### ***We've said it before and we'll say it again...financial reporting implications of an uncertain economy***

The projected “double-dip” recession hasn't materialized, but continued slow economic growth, the U.S. credit downgrade last August, and the ongoing European debt crisis are all contributing to an uncertain global economy. There are a number of financial reporting issues that can arise against this backdrop. We captured many of these issues in [Dateline 2011-27](#), *Financial reporting considerations stemming from an uncertain*

*global economy*, issued last quarter. That Dataline is worth a revisit as we head into the year-end reporting season. Here's a recap of some of the key areas.

### *Impairment assessments of investment securities*

The buzz phrase is “other-than-temporary impairment”—and it determines whether a decline in the value of an investment security should be recorded in earnings. How do you know if you have one? The answer depends on whether the investment in question is a debt or equity security. For a debt security, management must assess whether the company intends to (or may be forced to) sell the security prior to recovery. If not, only the decline in value related to credit losses is recognized in earnings. For equity securities, whether or not the company plans to sell the security isn't relevant. Instead, the assessment focuses on a number of qualitative factors, including the severity and duration of the impairment.

### *Previously impaired debt securities*

Think the hard work is done just because an impairment has been recorded? Think again. Accounting for previously impaired debt securities that have subsequently “recovered” a portion of their impaired value can be complex. Significant increases in the cash flows expected to be collected are generally treated as prospective yield adjustments. These securities also warrant extra attention to ensure they don't require additional impairment should cash flow expectations decline again.

### *Debt refinancings*

Don't be tempted by shortcuts here. Any debt refinancing first should be carefully assessed to determine whether it's a “troubled” debt restructuring. If the refinancing is not a “troubled” debt restructuring, the next step is to determine whether a modification or extinguishment has occurred. Each path down this decision tree has different accounting and reporting implications.

### *Use of forecasts*

While updating forecasts should be part of the regular routine, the need to refresh forecast assumptions becomes even more critical in an uncertain economy. Forecasted financial information is used for various financial reporting purposes. Such as? Changing forecasts could affect whether hedges of forecasted transactions continue to be effective. Changes in projected earnings or cash flows could also result in a “triggering event” requiring an impairment assessment of a long-lived asset, indefinite-lived asset, or goodwill. And, forecasts of future taxable income are integral to the assessment of the need for a valuation allowance on deferred tax assets.

### *Restructurings*

Companies focusing on reducing costs may consider various restructuring alternatives, such as lease modifications and workforce reductions. For many companies, restructurings don't happen that often, so when they do, it's important to revisit the guidance in this area. In particular, the accounting for a workforce reduction will depend on several factors, including whether the termination of employment is voluntary or involuntary and whether the termination benefits are a one-time benefit versus a payment made pursuant to an existing arrangement.

## Lower of cost or market...how low should you go?

The holiday season means one thing for consumers...bargains! Discounts and sales incentives seem to be more prevalent and offered earlier each holiday season, especially in today's economic environment. These discounts and incentives can also put more stress on inventory valuation assessments. Does offering a sales incentive indicate that existing inventory is impaired? Not necessarily, but here are some points to keep in mind.

Inventory is recorded at the lower of cost and market. "Market" is defined as the current replacement cost, but it should not exceed net realizable value (estimated selling price in the ordinary course of business less costs of completion and disposal). The net realizable value is not adjusted for declines in selling price that are temporary, such as a short-term holiday discount. However, sustained price declines (including discounts or incentives) might indicate that a decline is more than temporary. Determining the net realizable value of a product requires judgment, and all market data should be considered, even events subsequent to the balance sheet date.

Keep in mind that lower of cost and market can be applied on an item-by-item basis, by major category of products, or at any appropriate level that reflects a company's revenue stream. But it's not a "pick and choose" exercise—the test should be applied consistently from period to period.

## Pension plan remeasurements—an annual tradition

It's time again for many companies to perform their annual remeasurements of their pension and other postretirement benefit plan obligations. Of course, we can't let the year end go by without a few reminders in this area. What's in store for this year? The current economic environment continues to add a challenging dynamic to the assessment of the key assumptions to use in this annual analysis, including the discount rate and expected rate of return on plan assets.

For example, long-term interest rates continue to be at historic lows, which will likely factor into a company's discount rate assessment. On the asset side, the lingering effects of the recession and continued market volatility may indicate that companies should revisit their long-term view of asset return rates. Ditto for those companies that have recently rebalanced their plan asset portfolios to reduce risk. Bottom line: the double-whammy of low discount rates and the potential for lower asset return rates could translate into a higher net unfunded pension obligation for some companies.

The SEC had plenty to say about pensions at last week's AICPA conference, especially when it comes to disclosures. Transparent disclosures about future funding requirements and the plan asset portfolio, including any changes to investment strategy, topped the list.

Another issue brought-up by the SEC: recent decisions by some companies to change how they account for gains and losses related to pension plans. Disclosure, preferability, and the general guidance on changes in accounting policies are key considerations. For a refresher on this topic, see [Dateline 2011-03, Pension and OPEB accounting—Exploring changes in accounting policies](#), which we issued earlier this year.

Finally, don't forget that the new multiemployer pension plan disclosures are required this year for public companies. The timing is tight and employers that participate in these types of plans will need to collect additional information to comply with the requirements. Compiling the needed information may be particularly difficult for those

that participate in a large number of plans. For more information refer to [In brief 2011-33, FASB approves revised disclosures for multiemployer pension plans; effective for public companies in 2011.](#)

## **A closer look at the valuation of derivative instruments**

Methodologies utilized to value derivative instruments continue to evolve, even for “plain vanilla” products. Recently, some derivatives dealers have explored changes in the valuation of certain collateralized derivatives, including derivatives cleared through a central clearing house.

What’s being considered? To price a swap, valuation models estimate the cash flows the counterparties contractually agreed to pay each other over the life of the contract and apply a discount rate. Historically, that discount rate has been the London Interbank Offered Rate (LIBOR) rate. Some are exploring whether an overnight index swap (OIS) curve is more appropriate for certain collateralized derivative contracts. Historically, LIBOR moved in tandem with the OIS rates. However, during volatile markets, spreads between these rates can widen significantly. The larger difference between OIS and LIBOR and the availability of market data on OIS curves has prompted a closer look at the rates used in valuations.

Changes in valuation will impact both derivatives dealers and the counterparties to these trades. For a detailed look at the implications, see [Dataline 2011-30, Accounting for derivatives—Treasury and financial reporting implications of using an OIS \(not LIBOR\) curve in the valuation of certain derivatives.](#) For a discussion of valuation issues, see the [FS Viewpoint document](#) from PwC’s Financial Services Institute titled *It’s Harder Than You Think: The New Reality for Managing Risk and Valuation of OTC Derivatives.*

## **Who’s the principal? “Gross vs. net” revenue still a challenge**

The guidance for assessing whether to recognize revenue on a “gross” or a “net” basis is over a decade old. So, why is it a hot topic now? The issue originally arose during the internet boom, precipitated by the increase in the number of companies that act as resellers of goods or services. Now, new business models and types of transactions have emerged, bringing new revenue recognition challenges with them. For example, the sale of mobile device applications often involves multiple parties. There are also a number of companies that offer some form of online coupon or “deal of the day” promotions, which are typically fulfilled by other parties.

The starting point is to fully understand the company’s business model and all of the contractual arrangements between the parties involved. The accounting guidance<sup>3</sup> provides indicators that should be analyzed to assess which party is the principal in the arrangement. The principal recognizes revenue from a transaction on a gross basis (the amount billed to the customer), while an agent recognizes revenue net. However, the assessment is not a simple exercise of tallying up the indicators. While there are several indicators listed in the guidance, there are some that should be given more weight than others.

Which are the most important indicators? Assessing which party is the primary obligor will often—but not always—point to the party that is the principal in the arrangement. The primary obligor is the party responsible for fulfilling the ordered product or service. Another strong indicator is whether the company takes title to the product before it is ordered by the customer and therefore, holds inventory risk. The focus should not be on

<sup>3</sup> ASC 605-45, *Principal Agent Considerations*

how cash changes hands—whether the company physically receives the gross or net amount of cash is not determinative.

If you're stumped, there's no substitute for revisiting the accounting guidance and the "principal versus agent" indicators. The guidance also includes a number of examples that can be helpful when navigating the indicators.

## **Don't let unexpected compensation charges ruin your holidays**

While the accounting's not new, the frequency of equity restructurings and other stock transactions in recent periods has brought a few compensation issues back to the forefront. No one likes a surprise compensation charge—so read on, for some things to look out for.

### *Equity restructuring events*

An equity restructuring is a transaction such as a spin-off or nonrecurring large dividend that causes a company's stock price to change. It's typical in these situations for companies to modify the terms of stock options and other awards held by employees to adjust for the dilution caused by the restructuring event. The intent is to keep the employees "whole" after the restructuring event.

So, if employees are just being kept "whole," why would there be a compensation charge? There isn't, as long as the company was required to modify the awards. This is often the case, as many stock-based compensation plans include an "antidilution provision" that requires awards to be modified in these situations. In other fact patterns, a plan might be silent or give the board of directors or compensation committee discretion over whether to modify employee awards. A decision to modify awards that is not required by the plan results in the employees receiving something they weren't otherwise entitled to and therefore, usually results in a compensation charge.

Sometimes it's easy to tell if a plan requires a company to modify its employee awards in such a situation. But sometimes it's not. In those cases, management may want to consider speaking with legal counsel to assess what's required—before an equity restructuring is upon you like a long-lost relative.

### *Repurchases of stock from employees*

Other stock transactions involve purchasing shares from employees. In one fact pattern, common shares are purchased from existing shareholders, including employees, in connection with a preferred stock financing. This may be done to manage dilution or to provide liquidity to employees. The purchase might be done by the outside investor directly or the company may use cash from the financing to purchase shares.

The key factor in this scenario is determining the current fair value of the common shares—an assessment that often requires significant judgment. If the price paid for the shares exceeds their fair value, the excess is likely compensation. For many nonpublic companies, it may be prudent to have a valuation of the common shares performed by a third-party valuation firm. It's also worth noting that the company might be required to record compensation even if the outside investor purchases the shares from employees, if the investor is considered to be acting on behalf of the company.

## Who's got the power (to consolidate)?

Once upon a time, you could assume that consolidation would not be required so long as you owned less than 50% of an entity's voting equity. Those days are long gone now that there's guidance on variable interest entities (VIEs). So don't forget that this guidance needs to be assessed first, before considering the voting interest model.

Figuring out whether to consolidate a VIE can be tough, though. That's because consolidation depends on who has both the power to direct the activities of the VIE that most significantly impact the VIE's economic performance, and who has exposure to the VIE's economics. We'll have to save the economics discussion for another day, but here are a few pointers when thinking about who has the power.

- Be aware that power can come from many sources other than equity and governance. These sources can include management agreements and financing arrangements.
- Make sure you consider all relevant activities when identifying those that most significantly affect the VIE's economic performance. In some cases, a group of activities in the aggregate might be the most significant.
- Remember that whether an entity is a VIE and who should consolidate are decisions that should be reconsidered in certain circumstances, including when there has been an organizational, capital, or operational change.

Need a refresher on the VIE guidance? You may want to revisit [Dateline 2009-30, FAS 167—New consolidation guidance for variable interest entities](#) (an oldie but a goodie).

VIEs also came up at last week's AICPA conference. The SEC was focused on foreign VIE structures, but the key messages could be applicable to other VIEs as well. What will the SEC be on the lookout for? Depending on the fact pattern, relevant disclosures might include significant terms of contractual relationships with VIEs and information about operations outside of the VIE when the VIE represents the significant operations of the consolidated entity.

## Income tax disclosures continue to attract attention

We've hinted at the SEC's increased focus on income tax-related disclosures over the last year. Well, the topic was raised again at last week's AICPA conference. With this in mind, take note of the following when preparing those year-end disclosures.

### *Liquidity and capital resources*

Earlier this spring, we highlighted a recent trend in SEC comment letters that has now continued into the fall. Specifically, companies asserting indefinite reinvestment of foreign earnings are being asked to expand their management discussion and analysis to more clearly describe how this assertion may impact their businesses, especially liquidity. And again, at the AICPA conference, the SEC outlined specific disclosures it would expect to see in this situation, including the amount of cash and short-term investments held by foreign subsidiaries that is not available without a cost to fund domestic operations.

### *Effective tax rate reconciliation*

The SEC continues to ask companies for more information regarding the composition of their annual effective tax rates, with a particular interest in items related to foreign activity. For example, the SEC has asked for more detail regarding the effect of having proportionally higher earnings in jurisdictions with lower statutory tax rates. At the

AICPA conference, the SEC touched on this issue as well and suggested it may be appropriate to disclose if the proportion of earnings subject to lower tax rates is expected to change in the future.

### *Realizability of deferred tax assets*

Valuation assessments continue to attract attention from the SEC. This isn't surprising given the judgment required in this area. In particular, the SEC is interested in how a company weighs positive and negative evidence and the events leading up to either recording or releasing a valuation allowance. The SEC also reiterated at the AICPA conference that cumulative losses in recent years represent significant negative evidence that may be difficult to overcome.

### **Transfer pricing—it's more than an agreement between friends**

The topic of transfer pricing and its impact on financial reporting is often associated with uncertain tax positions. However, transfer pricing can have other financial reporting implications. For example, transfer pricing arrangements between related parties may play a key role in assessing a company's deferred tax assets for realizability. A company's transfer pricing policies also directly affect the calculation of its estimated annual effective tax rate.

Other areas affected by transfer pricing include business restructurings, the measurement of deferred taxes on foreign earnings, separate company financial statements, and disclosures. Have we piqued your interest? Our recent publication, [Tax Accounting Services: The impact of transfer pricing in financial reporting](#), takes a closer look at this topic.

### **It's déjà vu all over again as key U.S. tax provisions are set to expire**

Here we are again, facing the potential expiration of several longstanding beneficial corporate tax provisions, such as the federal research credit and provisions deferring the taxation of certain foreign earnings. It's a year later and the message is just about the same...and it's not because we've run out of material. Although Congress ultimately took legislative action and reinstated the tax provisions into law for the 2010 tax year, many of these same provisions are scheduled to expire on December 31, 2011. With 2012 around the corner, the fate of the expiring provisions remains unclear.

So, what are the implications? Companies that benefit from the foreign earnings deferral provisions will need to consider how the scheduled expiration will affect the year-end measurement of deferred taxes and key financial statement assertions, such as indefinite reinvestment. These assessments should be based on the tax law in effect on the balance sheet date, without assuming the provisions will be reinstated. Further, companies that have historically benefited from the federal research credit should consider the impact of the expiration when establishing their estimated annual effective tax rates for 2012. And remember, if changes are enacted after year-end, but before the issuance of financial statements, companies should consider disclosing the impact. For more discussion of the foreign earnings deferral provisions, see [Tax Accounting Services NewsAlert, Tax accounting considerations related to lapsing Subpart F provisions](#).

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## Hot off the press

### Current FASB proposals:

Out for comment	Comment deadline
Technical corrections	December 13
Accounting for CTA (EITF consensus)	February 6
Investment property entities	February 15
Investment companies	February 15
Consolidation: principal vs. agent	February 15
Revenue recognition	March 13

### FASB grants wish for deferral of new other comprehensive income reclassification requirement

Word travels fast. Preparers let the FASB know that the new requirement to show reclassifications from other comprehensive income to net income by line item on the face of the financial statements was causing some major heartburn. The FASB took quick action and agreed to defer that specific requirement...but not the entire standard.

What's the issue? Reclassifications from other comprehensive income can affect multiple line items within net income. For example, reclassification of pension-related amounts could affect any line item that includes compensation. Also, some reclassification amounts might initially be capitalized (for example, as inventory). The new standard on presenting other comprehensive income requires presentation of these classifications by line item on the face of the financial statements. Not only does this create additional work for preparers, some believe it adds unnecessary complexity and "clutter" to the income statement. The deferral will allow the FASB time to further research how best to provide investors with greater clarity about the impact of reclassification adjustments on net income.

As a reminder, all of the other requirements of the standard are unaffected by the deferral. The standard is effective for public companies in 2012. See [In brief 2011-48](#), *FASB issues proposal to defer new presentation requirement for other comprehensive income reclassifications*, for more information.

### New goodwill guidance—perhaps the FASB's most popular standard ever

Just days after releasing our last edition of *The quarter close*, the FASB finalized its popular proposal to simplify the goodwill impairment test. As a reminder, the revised guidance is intended to reduce the cost and complexity of the annual goodwill impairment test by providing both public and nonpublic companies with the option of performing a "qualitative" assessment to determine whether further impairment testing is necessary. The revised standard is effective for goodwill impairment tests performed in 2012. A company can choose to adopt the standard early provided that it has not yet issued its financial statements for the period that includes its annual test date.

Even if you don't plan to adopt early, it's a good idea to start thinking about disclosures. Goodwill impairment has long been an area of focus for the SEC, and comments at last week's AICPA conference only reinforced this point. One key takeaway: the SEC will be looking for full and transparent disclosure of how companies are applying the qualitative assessment.

For more information, see [Dataline 2011-28](#), *Goodwill impairment—FASB issues guidance that simplifies goodwill impairment test and allows early adoption*. You also might want to check out our archived [webcast](#), where we provide insights and tips on applying the revised guidance.

### *New practice aids for goodwill and IPR&D on the way*

Speaking of goodwill, the AICPA's Financial Reporting Executive Committee recently issued exposure drafts updating two of its popular Accounting and Valuation Guides. The first guide covers goodwill impairment, while the second addresses the valuation of

research and development activities acquired in a business combination. The updates reflect changes in both accounting standards and valuation practices since the guides were first issued. Although not authoritative, these guides have proven helpful to financial statement preparers, auditors, and valuation practitioners alike. Comments are due by March 15.

## **Revenue recognition—did they get it right?**

When it comes to the revenue recognition project, there's one thing everyone can agree on: revenue is one of the most important, closely scrutinized measures in a company's financial statements. That's one reason the FASB and IASB decided to re-expose their proposal. The core principle has not changed from the June 2010 proposal: an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled. But, there have been changes to the guidance on how to apply the core principle, primarily in response to feedback received during the comment letter process and the boards' outreach efforts.

The FASB's not calling it a wrap just yet. FASB Chairman Leslie Seidman announced this quarter that in addition to re-exposure, the FASB plans to continue "field testing" of the proposal. This will include workshops for companies in certain industries, and review of "before and after" mock-ups of common transactions to assess how companies interpret the guidance and to key in on any unintended consequences of the proposed standard.

The boards received almost 1,000 responses to their first exposure draft. Will the revised exposure draft generate the same level of interest? It remains to be seen, but don't miss your opportunity to weigh in. The deadline for comments is March 13. For more information on the exposure draft, including helpful examples and insights (along with several industry-specific supplements), see [Dateline 2011-35, Revenue from contracts with customers—The proposed revenue standard is re-exposed](#). You can also access our archived [webcast](#) that summarizes the proposed guidance, along with commentary from a panel of experts, including the revenue project manager at the FASB.

## **"Trio" of exposure drafts addresses consolidation and investment accounting topics**

The FASB issued not one, not two, but three exposure drafts this quarter that address certain (sometimes overlapping) issues related to consolidations, investment companies, and investment property entities. Having trouble keeping them straight? Here are the cliff notes:

### *Consolidation: principal versus agent*

These targeted changes to the consolidation model will end the deferral of the current consolidation guidance for certain investment entities<sup>4</sup>. The proposal introduces a "principal versus agent" assessment to be performed by a reporting entity that has decision-making authority over another entity. The decision maker will assess whether it uses its authority to act as a principal or an agent. A decision maker acting as a principal consolidates the other entity, while a decision maker acting as an agent generally does not. In many respects, the proposal is largely consistent with guidance in the IASB's recently issued consolidation standards.

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<sup>4</sup> Certain investment entities were granted a deferral from applying FAS 167, *Amendments to FASB Interpretation No. 46(R)* (codified in ASC 810).

### *Investment companies*

This proposal amends the definition of an “investment company.” One big change: entities that do not hold multiple investments or only have a single investor will no longer qualify for investment company accounting. Entities that are registered under the Investment Act of 1940 will automatically qualify as an investment company. Investment companies will account for their portfolio investments at fair value even when they have a controlling interest in an investee. However, the proposal requires investment companies to consolidate other investment companies and investment property entities they control—a significant change from current practice. The IASB issued a similar proposal, albeit with some key differences from the FASB’s proposal.

### *Investment property entities*

This proposal defines an “investment property entity” (using criteria that, in many ways, are similar to that proposed for investment companies) and requires these entities to record their investment properties at fair value. The FASB originally took on this project in conjunction with the joint project on lease accounting. The initial lease accounting proposal included a scope exception for lessors that record investment property at fair value. This quarter, the boards tentatively decided to expand this scope exception, effectively eliminating the interplay between the two projects.

### *For more information...*

The original comment letter periods for these proposals were pretty tight, and many respondents said they needed more time to digest the exposure drafts. So just last week, the FASB delivered an early holiday present: comments on all three proposals now are not due until February 15.

You may have noticed that these projects address some complex topics. You can find more information in our December edition of *Setting the standard*. And, for a deeper dive into the proposals, see the following Datalines: [Dataline 2011-33, Consolidation of VIEs and partnerships—more changes under consideration](#); [Dataline 2011-32, Investing in a new investment company definition](#); and [Dataline 2011-34, Investment property entities—The good, the bad, and the ugly](#).

## **EITF votes to retain narrow scope in new deconsolidation guidance**

In our [third quarter edition](#) of *The quarter close*, we described a complicated issue taken on by the EITF related to deconsolidation of real estate entities. As a refresher, this issue addresses the accounting for the deconsolidation of an entity that is primarily comprised of real estate and whether the consolidation guidance or real estate sales rules should govern. The EITF released a consensus-for-exposure in July, which gave the nod to the real estate sales guidance. The consensus was limited to a narrow fact pattern, specifically the investor’s accounting when it loses control to a lender in a default situation. In November, the EITF’s consensus was finalized and ratified by the FASB. The new guidance will be effective for public companies for fiscal years beginning after June 15, 2012.

Reaching a final consensus on this issue was not a slam dunk. At its November meeting, the EITF discussed feedback from respondents, which included concerns about the narrow scope of the issue, particularly the lack of guidance from a lender’s perspective. Those concerns were echoed by several EITF and FASB board members.

In a close vote, the EITF decided to affirm its initial consensus, but recommended that the FASB add a separate issue to its agenda to address the lender's accounting for these transactions. Instead of adding a separate project specifically on lender accounting, the FASB decided to add a research project to its agenda to examine broader issues about whether to apply "asset-based" or "entity-based" guidance to nonfinancial assets held by a reporting entity. For more background on this issue, see the November 2011 [EITF observer](#).

### **Foreign currency accounting—EITF takes a step toward reducing diversity**

At its November meeting, the EITF discussed the newest issue on its agenda: what should happen to a parent company's cumulative translation adjustment when it sells a business that's part of—but not an entire—foreign entity? That is, should the cumulative translation adjustment related to the business be released into earnings upon sale? Currently, a conflict exists between the deconsolidation guidance and foreign currency guidance in this area.

It didn't take the EITF long to conclude that a reasonable solution was to allow for a release of the cumulative translation adjustment related to the business into earnings in these situations. In other similar transactions, such as a parent's loss of control of a subsidiary, the related cumulative translation adjustment is released into earnings. The EITF decided that the accounting for the sale of assets constituting a business should receive the same treatment.

A follow on issue is how an entity should allocate the cumulative translation adjustment into earnings: relative fair value, relative book value, specific identification, or some other basis? The EITF decided not to provide prescriptive guidance on this issue other than to say a systematic and rational approach should be utilized. That's good news since many companies track these balances differently.

The EITF will discuss effective date and transition after receiving feedback during the comment period, which ends on February 6. For more information, see the November 2011 [EITF observer](#).

### **FASB crosses t's and dots i's—Codification technical corrections**

A little housecleaning now and then is always a good idea. The FASB's clean-up efforts came in the form of an exposure draft that corrects minor technical matters and conforms the use of the term "fair value" throughout the codification of U.S. GAAP. The intent is not to significantly change current guidance; however, certain corrections could be more substantive than others. For example, healthcare entities may want to focus on the proposed changes to the accounting for advance fees for continuing care retirement communities. The comment period ends on December 13. For more information, see [In brief 2011-42](#), *FASB publishes exposure draft on Codification Technical Corrections project*.

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## **SEC matters**

The SEC is back to its full complement of five commissioners with Daniel Gallagher<sup>5</sup> joining the ranks in November. And it's a good thing, because there's no shortage of items on the SEC's agenda. At last week's AICPA conference, the SEC recapped the many rules and other forms of guidance it issued over the past year. This pace is not expected to slow any time soon. In particular, the SEC plans to make further progress in 2012 on rulemaking to implement the Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Among the rules expected next year: disclosure requirements for conflict minerals and executive compensation. We discussed these pending rules in our [third quarter edition](#) of *The quarter close*.

The SEC also introduced a new form of guidance this quarter dubbed "Corporation Finance Disclosure Guidance." We highlight below the first two topics addressed in this format: cybersecurity risks and reverse mergers.

### **SEC weighs in on cybersecurity risks**

Cyber attacks and data breaches have emerged as a significant business risk for many companies, as evidenced by the high-profile cyber attacks making news this year. Now the SEC has weighed in on how registrants should be disclosing these risks in their financial statement filings. The SEC provided its views as part of its new disclosure guidance series.

There's no disclosure requirement in place today that explicitly refers to cybersecurity risks. However, the SEC pointed out that a number of existing requirements may impose an obligation on registrants to disclose such risks and cyber attack incidents. These requirements could affect multiple sections of SEC filings including risks factors, management discussion and analysis, and financial statement disclosures. For more information, see the SEC's disclosure guidance on the SEC's [website](#).

Interested in more on cybersecurity? For more on the broader topic of information security, see our [2011 Global economic crime survey](#), which includes an in-depth look at cybercrime, and [10Minutes on information security](#).

### **SEC kicks off new roundtable series**

In November, the SEC held its first session of an ongoing series of roundtables (referred to as the "Financial Reporting Series") designed to get feedback on financial reporting matters. Participants at these roundtables will include a cross section of capital market participants: investors, preparers, and auditors. The SEC's goal is to use the information gained from the roundtables to proactively address difficult financial reporting issues. Representatives from the PCAOB and FASB will also attend so that issues can be evaluated using a holistic approach.

The first roundtable was focused on the extent to which financial reporting should include measurement uncertainties (for example, measurements based on judgments and models), and the information investors find important to understanding and assessing those uncertainties. What were the takeaways? Primarily, the importance of

***We intend for the financial reporting series to become a critical and ongoing part of the SEC's work to protect investors and enhance our capital markets.***

-Mary L. Schapiro, SEC  
Chairman, [November 8, 2011](#)

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<sup>5</sup> Commissioner Gallagher worked at the SEC from 2006-2010, serving as a counsel to prior Commissioners and as Deputy Director of the Division of Trading and Markets. He left the SEC in early 2010 to become a partner in the Washington, D.C. office of WilmerHale, and was appointed as an SEC Commissioner by President Obama in October 2011.

clear, understandable communication to investors. The archived webcast of the roundtable is available on the SEC's [website](#).

## **XBRL liability limitations begin to sunset**

The XBRL requirements are now effective for all U.S. public companies. So, what's the next notable milestone for XBRL? This year, companies in the first phase-in group begin to lose the protections of the modified liability provisions. These provisions protect companies from liability so long as they make a good faith effort to comply with the tagging requirements and correct errors promptly. But this "safety net" generally expires two years after a company's first XBRL submission. After that, a company's interactive data submissions are subject to the same liability provisions as the financial statements included in its "official" filing.

It's no surprise then that many companies are placing renewed emphasis on getting their XBRL submissions right. A growing number of these companies are taking it a step further, and are exploring having a third party perform agreed-upon procedures on their interactive data. To learn more, refer to the PCAOB's [Staff Questions and Answers, Attest Engagements Regarding XBRL Financial Information Furnished under the XBRL Voluntary Financial Reporting Program on the Edgar System](#).

## **SEC and U.S. exchanges tighten the reins on reverse merger companies**

The SEC has been keeping a close eye on companies accessing the U.S. markets through reverse mergers. The SEC and U.S. exchanges have recently suspended or halted trading in a number of companies that were formed by reverse mergers. Back in June, the SEC issued an investor bulletin warning investors about the risks associated with reverse mergers, citing instances of fraud and other abuses. And now, the SEC has approved new rules proposed by the three major U.S. exchanges designed to toughen listing standards for these companies.

So, what exactly is a reverse merger? A reverse merger allows a private company to access the U.S. markets by merging with an existing public "shell company" with few or no operations. The private company is therefore able to avoid the lengthy, complex, and expensive process of going public, and the scrutiny that accompanies the process. But that's likely to come to an end under the new rules. The new rules prohibit a reverse merger company from applying to list on the three major U.S. exchanges until the company has completed a one-year "seasoning period" by trading in the U.S. over-the-counter market or on another regulated U.S. or foreign exchange, and maintained a minimum share price for a sustained period of time.

The SEC also provided observations this quarter on the filings used to report reverse mergers and similar transactions as part of its new disclosure guidance series. The observations include several areas in which the SEC has frequently reminded companies of the disclosure requirements or asked for enhanced disclosures. The guidance can be accessed on the SEC's [website](#).

Continuing on this theme, the SEC continues to ask questions about whether companies with operations outside of the United States have the sufficient knowledge and capability to prepare U.S. GAAP financial statements. We discussed these comments in our [second quarter edition](#) of *The quarter close*, and these messages were reiterated by the SEC at last week's AICPA conference.

***Placing heightened requirements on reverse merger companies before they can become listed on an exchange will provide greater protections for investors.***

- Mary L. Schapiro, SEC Chairman, [November 9, 2011](#)

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## ***IFRS developments***

### **SEC's assessment of IFRS continues**

***We believe in the vision—a single set of high quality, transparent and robust global accounting standards.***

- PwC [Point of view](#), *The path forward for international standards in the United States*

We already broke the news. Yes, the SEC had anticipated making a final determination by the end of 2011 about whether, when, and how to incorporate IFRS into the U.S. financial reporting system. But, it appears that decision will not come this year after all. The delay shouldn't be surprising, though. When it announced the work plan and timetable in early 2010, the SEC indicated that one factor in any decision would be whether the FASB and IASB had made sufficient progress on their priority convergence projects, many of which have since been delayed. In his remarks at last week's AICPA conference, SEC Chief Accountant Jim Kroeker also emphasized the importance taking the time to establish a "strong and lasting framework" to ensure, among other things, a strong U.S. voice in global accounting standard setting.

In the meantime, the SEC's May 2011 paper on a possible method of incorporation continues to generate discussion. The paper explores an endorsement approach that would change U.S. GAAP over a period of five to seven years by incorporating individual international standards into U.S. GAAP. In our [third quarter edition](#) of *The quarter close*, we summarized feedback on the paper, much of which has been positive.

***We always are going to need a nimble, responsive body to address important matters in the U.S.***

- Leslie F. Seidman, FASB Chairman, [December 6, 2011](#)

Recently, the FAF gave its views through a comment letter to the SEC that generally supported the endorsement approach. But the FAF warned against "too much, too soon" when it comes to turning over authority for U.S. standard setting to an international body, and suggested retaining a robust role for the FASB in the standard-setting process. FASB Chairman Leslie Seidman expanded on the FAF's views during last week's AICPA conference. She suggested it may be necessary for the IASB to re-examine certain IFRS standards prior to incorporation into U.S. GAAP. She also pointed out that current U.S. GAAP may need to be retained in areas that IFRS guidance does not cover. For example, guidance for rate regulated entities currently exists in U.S. GAAP, but not IFRS.

On IASB Chairman Hans Hoogervorst's wish list: an option for U.S. companies to early adopt IFRS. During his address at the AICPA conference, he explained why the ability to early adopt would be beneficial and encouraged the SEC to allow for this option. Some U.S. companies have provided similar feedback to the SEC. It's unlikely, though, that an option to early adopt IFRS will be in anyone's stocking...at least this year.

We provide our views on IFRS incorporation in our recent [Point of view](#), *The path forward for international standards in the United States—considering possible alternatives*.

### ***SEC issues two papers on IFRS***

The SEC made progress on its IFRS work plan by issuing two additional papers in November. The first paper compares existing U.S. GAAP to IFRS. In the second paper, the SEC analyzes IFRS financial statements prepared by companies in the Fortune Global 500 to assess the consistency of the application of IFRS.

What were the findings? At a high level, the findings likely confirm what many expected to hear. For example, the comparison of U.S. GAAP and IFRS revealed that U.S. GAAP contains more detailed guidance as a result of industry or transaction-specific standards that are absent in IFRS. When it comes to consistency of applying IFRS, the SEC noted diversity across territories and identified the need for more transparent financial statement disclosures.

No specific conclusions were reached in the papers. Instead, they are designed to provide information relevant to the debate and to facilitate the SEC's decisions about incorporating IFRS. For more information on the two papers, refer to [Dataline 2011-36](#), *SEC Staff continue progress on IFRS work plan—Comparison between IFRS and US GAAP frameworks and analysis of IFRS in practice*.

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## ***On the horizon***

### **Lessors of investment property might get a path of least resistance**

Just when it appeared to be about wrapped-up, the FASB and IASB's joint project on lease accounting continues to be easier said than done. Most of the discussions this quarter have centered on the lessor accounting model. One of the bigger challenges: leases of investment property. The original exposure draft provided a scope exception for lessors that record investment property at fair value. This prompted the FASB to take on a project to define when an entity should record investment property at fair value (we discuss the resulting exposure draft in "Hot off the press"). Now the boards have tentatively decided to expand this scope exception to include all lessors of investment property, whether or not such property is carried at fair value.

Where does that leave lessor accounting? Effectively, there will be two models: one for leases of investment property and the other for leases of equipment and other assets. Lessors of investment property will continue to apply today's "operating lease" accounting, while lessors of other assets will apply the "receivable and residual" approach in the new standard. In addition to the difference in balance sheet presentation, a key difference between the two approaches is the pattern of revenue recognition—the "receivable and residual" approach results in a downward sloping pattern of revenue recognition.

Sound familiar? The boards had explored a two model approach to lessee accounting, but had encountered several implementation issues. They eventually settled on a single model approach for lessees. Some have questioned why lessors should get an exception for investment property, but lessees should not have a similar exception in lessee accounting. The boards may discuss this issue further before issuing the revised exposure draft.

The boards tentatively agreed that preparers could apply either a full retrospective application of the standard or a modified transition approach. The modified transition approach is intended to ease the burden of initial application and to mitigate to some extent the "front-end loading" of lease expense at the transition date.

When will you get your chance to chime in on these decisions? A revised exposure draft is expected in the first half of 2012. We provide more highlights of the project in our December edition of *Setting the standard*, coming soon. For a summary of the latest significant decisions, see [In brief 2011-44](#), *FASB and IASB make significant decisions related to lessor accounting and transition*.

## **The financial instruments project—where does it stand?**

Well, not much has changed since our last update. The FASB’s public discussions on the financial instruments project have been limited this quarter. A revised classification and measurement proposal is expected, but there’s been no official word on re-exposure just yet. Timing of the FASB’s re-exposure of impairment and hedging is also still very much up in the air. However, behind the scenes, the FASB and IASB have been working feverishly on their new impairment model. We expect further discussions by the boards on the model later this week month.

Meanwhile, there have been some noteworthy developments at the IASB. Last quarter, the IASB postponed the effective date of its standard on classification and measurement<sup>6</sup>. Now, the IASB has announced that the standard will be reopened for limited improvements, in part to consider bridging differences with the FASB’s proposal.

The IASB has also kicked-off discussions on macro-hedging. Macro-hedging refers to hedging risks in “open” portfolios—portfolios where the population can continue to change over time. Macro-hedging is not currently permitted under U.S. GAAP, but many U.S. companies are hoping the FASB will pick-up this topic as well. These companies will no doubt have a keen interest in the IASB’s decisions in this area.

For more updates on the financial instruments project, see our December edition of *Setting the standard*.

## **FASB agrees to extend “qualitative” test to indefinite-lived intangibles**

Folks just can’t seem to get enough of the new “qualitative” goodwill impairment assessment. And the FASB—knowing a good thing when they see it—appears ready to extend a similar qualitative option to indefinite-lived intangibles. You might recall that many who responded to the goodwill exposure draft pointed out that testing indefinite-lived intangibles for impairment often takes as much effort as goodwill, primarily because both tests use many of the same underlying projections as a starting point.

This quarter, the FASB discussed a proposed qualitative approach similar to the approach for goodwill, and using the same qualitative factors. The factors would be used to determine if it is more likely than not that an indefinite-lived intangible asset’s fair value is less than its carrying amount. And the potential stocking stuffer? It’s expected that companies will be able to early adopt the new guidance, once issued.

The project is on the fast track, so expect to see an exposure draft soon. It’s likely that the qualitative test for indefinite-lived intangibles will be available to companies as early as 2012.

## **Debate continues on auditor’s report and auditing profession**

Feedback is coming in on the PCAOB’s two concept releases issued earlier this year. As a quick refresher, the first release focuses on auditor’s reporting and the second explores ways to enhance auditor independence, objectivity, and professional skepticism, including mandatory audit firm rotation.

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<sup>6</sup> The IASB’s standard providing classification and measurement guidance for financial instruments (IFRS 9, *Financial instruments*) was originally effective for annual periods beginning on or after January 1, 2013. The IASB proposed in August to delay the effective date to annual periods beginning on or after January 1, 2015.

The PCAOB held a roundtable on the auditor's reporting model in September, and comments were due on the concept release at the end of that month. The feedback? A mixed bag—not surprising, considering the many different stakeholders involved. While most agree the auditor's report could benefit from some changes, many question whether a full blown auditor's discussion and analysis would be practical—or even appropriate, given the auditor's role. The PCAOB has indicated that it plans to issue a proposal on this topic in the second quarter of 2012.

***[Term limits] is not an easy subject... Comments have been flowing in. Please submit yours.***

-James R. Doty, PCAOB Chairman, [December 5, 2011](#)

When it comes to mandatory audit firm rotation, views are mixed, but many are unconvinced that term limits will increase audit quality. A speaker from the SEC at last week's AICPA conference pointed out that a preliminary analysis appears to show no correlation between audit tenure and the number of comments in PCAOB inspection reports. In his address, PCAOB Chairman James Doty encouraged those opposed to the idea of term limits to provide alternative solutions. There's only a day or two left to weigh in on this concept release—the official comment period ends December 14. However, at least one PCAOB member said recently that he will read all letters—even those received after the cut-off date. Finally, don't forget that the PCAOB plans to hold a roundtable this upcoming March on mandatory audit firm rotation.

For more information on the PCAOB's concept releases, refer to [In brief 2011-29, PCAOB explores possible changes to the auditor's reporting model](#), and [In brief 2011-35, PCAOB seeks comment on auditor independence and audit firm rotation](#).

#### *What's in a name? PCAOB proposes that audit report identify the lead partner*

The PCAOB added another issue to the mix with a proposed standard that would require audit firms to disclose in the audit report the name of the lead engagement partner and certain other participants involved in the audit. You may recall that the original concept release in 2009 explored whether the lead engagement partner should personally sign the audit report. In proposing that the engagement partner be identified in (but not sign) the audit report, the PCAOB appears to be searching for a middle ground. Comments are due on the proposal by January 9.

#### *What happens in Europe stays in Europe...or does it?*

Many of the topics addressed in the PCAOB releases are also being debated internationally. At the end of November, the European Commission released a much anticipated—and controversial—proposal to reform the audit market. The proposed legislation will take time as it will be subject to additional process and debate before final legislation is adopted. Some of the more significant elements of the proposal include:

- Audit firms would be subject to term limits of six years, including a four year “cooling off” period before an audit firm could again audit the same company. Although the proposal ultimately did not include a requirement for joint audits, it does allow companies that voluntarily choose joint audits to retain their audit firms for up to nine years.
- Audit firms would be prohibited from providing non-audit services to their audit clients. In addition, large audit firms would be required to separate their audit businesses from non-audit activities to minimize perceived conflicts of interest.

These developments may relate to auditing policies and practices in the European Union, but they could have implications in other geographies as well, including the United States. Multinational companies with operations in Europe would be directly affected if their European subsidiaries are subject to the European Commission's rules. And it's

becoming clear that public policy ideas are no longer limited by regional boundaries and can be easily exported. Developments in Europe may influence regulators in the United States to consider similar changes.

### **“Going concern” project—back under a new name**

What “going concern” project? We’ll understand if you’ve forgotten that this was even on the FASB’s agenda, considering the original exposure draft was issued back in 2008. Bearing the new moniker “Disclosures about Risks and Uncertainties and the Liquidation Basis of Accounting,” the project got a jump start this quarter when the FASB directed its staff to perform more outreach with preparers, auditors, and other stakeholders in order to redefine the scope of the project.

Speaking of scope, the FASB appears to have decided that improving “early warning” disclosures should not be an objective of the project. Why? The FASB believes the main benefits of such disclosures will be achieved through the incremental disclosures about liquidity risk now included in the separate financial instruments project. One of the project’s more controversial aspects—still under debate—is whether management should be required to make an assertion about whether the company will continue as a going concern. Some believe that management lacks the objectivity to make such an assessment. Maybe, maybe not...but the answer might depend in large part on whether the FASB can come up with an operable definition of “substantial doubt.”

In any case, the FASB will need to coordinate its efforts with other parties, including the PCAOB, the AICPA’s Auditing Standards Board (ASB), and the SEC. That’s because going concern evaluations have long been part of the auditing standards. In fact, the ASB recently released an exposure draft updating its auditing standard<sup>7</sup> on going concern that would, among other things, require the auditor to obtain written representations from management if conditions or events have been identified that indicate there could be substantial doubt about an entity’s ability to continue as a going concern.

Now that discussions about the priority standard-setting projects are winding down, expect more focus on this project in 2012. An exposure draft is currently slated for the first half of the year.

### **First look at updated COSO framework coming soon**

It’s been nearly twenty years since the Committee of Sponsoring Organizations of the Treadway Commission (COSO) published its guidance providing a framework for internal controls. In that time, the COSO framework has become ubiquitous as the standard by which most public companies—and many private companies—design and evaluate their systems of internal control. But, it’s an understatement to say things have changed since the original guidance was issued. So it’s only appropriate that COSO plans to release a draft of an updated framework soon.

The update won’t change the framework’s five core components, but might change how the components are applied. All interested parties will have a chance to comment on the draft updated guidance. COSO expects to publish final guidance in two parts in the second quarter of 2012. The first document will be an updated overall framework, while the second will include more specific guidance on applying the framework to financial reporting objectives.

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<sup>7</sup> AICPA Professional Standards (AU sec. 341 and AU-C sec. 570)

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## **Corporate governance**

### **What's next for proxy access?**

The courts struck down mandatory proxy access last quarter, but that doesn't mean the debate on proxy access is over. Without much fanfare, the SEC's "other" rule on proxy access (an amendment to Rule 14a-8, also called "private ordering") became effective in September. This rule takes a different approach. It allows shareholders to submit proposals to allow proxy access on a company-by-company basis. If successful, shareholders could then in the subsequent year propose their own director nominees for inclusion in the company's proxy materials.

For more discussion, including some steps directors can take to prepare for the upcoming proxy season, see the Fall 2011 edition of *To the point* on our [Corporate Governance website](#). Proxy access was also discussed on a recent [BoardVision series](#) episode, presented with the National Association of Corporate Directors.

### **PwC Annual Corporate Director Survey**

Our recently issued *Annual Corporate Director Survey* marks the tenth year of this publication. The survey reflects the intelligence we've gathered from more than 800 directors. This year, the survey results include directors' views on executive compensation and how those views have changed in light of the "say on pay" rules that were effective for the 2011 proxy season. Other hot topics include risk management, succession planning, and diversity. Access the survey results on our [Corporate Governance website](#). The results are also highlighted in our recent [10Minutes document](#), *10Minutes on the boardroom agenda*.

### **BoardroomDirect**

The Fall 2011 edition of *BoardroomDirect* provides directors with recommendations on what works best in the boardroom, based on research we performed and describe in our report, *Board Effectiveness – What works best*, 2nd edition. This publication is available on our [Corporate Governance website](#).

***Directors are facing increased scrutiny from shareholders, regulators, and other stakeholders.***

- Don Keller, partner in PwC's Center for Board Governance

## Appendix

### Effective dates for recently issued standards

ASU 2010-06, <i>Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements</i>	Interim and annual periods beginning after December 15, 2009 <sup>8</sup>
ASU 2010-20, <i>Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses</i>	Interim and annual reporting periods ending on or after December 15, 2010 <sup>9</sup>
ASU 2010-13, <i>Compensation—Stock Compensation (Topic 718): Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Currency of the Market in Which the Underlying Equity Security Trades</i>	Fiscal years (including interim periods) beginning on or after December 15, 2010
ASU 2010-15, <i>Financial Services—Insurance (Topic 944): How Investments Held through Separate Accounts Affect an Insurer’s Consolidation Analysis of Those Investments</i>	Fiscal years (including interim periods) beginning after December 15, 2010
ASU 2010-16, <i>Entertainment—Casinos (Topic 924): Accruals for Casino Jackpot Liabilities</i>	Fiscal years (including interim periods) beginning on or after December 15, 2010
ASU 2010-24, <i>Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries</i>	Fiscal years (including interim periods) beginning after December 15, 2010
ASU 2010-28, <i>Intangibles—Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts</i>	Fiscal years (including interim periods) beginning after December 15, 2010 <sup>10</sup>
ASU 2010-29, <i>Business Combinations (Topic 805): Disclosures of Supplementary Pro Forma Information for Business Combinations</i>	Business combinations with an acquisition date on or after the beginning of the first annual reporting period beginning on or after December 15, 2010
ASU 2011-01, <i>Receivables (Topic 310): Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20</i>	As of January 19, 2011

<sup>8</sup> The disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements are deferred until fiscal years beginning after December 15, 2010, including interim periods.

<sup>9</sup> For public entities, the disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. [Note: Refer to ASU 2011-01 for deferral of the effective date for disclosures about troubled debt restructurings.] For nonpublic entities, all disclosures are effective for annual reporting periods ending on or after December 15, 2011.

<sup>10</sup> For nonpublic entities, the amendments are effective for fiscal years beginning after December 15, 2011, including interim periods.

ASU 2010-23, <i>Health Care Entities (Topic 954): Measuring Charity Care for Disclosure</i>	Fiscal years beginning after December 15, 2010
ASU 2010-27, <i>Other Expenses (Topic 720): Fees Paid to the Federal Government by Pharmaceutical Manufacturers</i>	Calendar years beginning after December 31, 2010
ASU 2011-02, <i>Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring</i>	First interim or annual period beginning on or after June 15, 2011 <sup>11</sup>
ASU 2011-09, <i>Compensation—Retirement Benefits—Multiemployer Plans (Topic 715-80): Disclosures about an Employer's Participation in a Multiemployer Plan</i>	Fiscal years ending after December 15, 2011 <sup>12</sup>
ASU 2010-26, <i>Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts</i>	Fiscal years (including interim periods) beginning after December 15, 2011
ASU 2011-03, <i>Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements</i>	First interim or annual period beginning on or after December 15, 2011
ASU 2011-04, <i>Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs</i>	Interim and annual periods beginning after December 15, 2011 <sup>13</sup>
ASU 2011-05, <i>Comprehensive Income (Topic 220): Presentation of Comprehensive Income</i>	Fiscal years (including interim periods) beginning after December 15, 2011 <sup>12</sup>
ASU 2011-07, <i>Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities</i>	Fiscal years (including interim periods) beginning after December 15, 2011 <sup>12</sup>
ASU 2011-08, <i>Intangibles—Goodwill and Other (Topic 350): Testing Goodwill for Impairment</i>	Goodwill impairment tests performed for fiscal years beginning after December 15, 2011
ASU 2011-06, <i>Other Expenses (Topic 720): Fees Paid to the Federal Government by Health Insurers</i>	Calendar years beginning after December 31, 2013

<sup>11</sup> The amendments should be applied retrospectively to the beginning of the annual period of adoption. For nonpublic entities, the amendments are effective for annual periods ending on or after December 15, 2012, including interim periods.

<sup>12</sup> For nonpublic entities, the amendments are effective for the first annual period ending after December 15, 2012.

<sup>13</sup> For nonpublic entities, the amendments are effective for annual periods beginning after December 15, 2011.

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**Edited by:**

**Jan Hauser**

Partner

Phone: 1-973-236-7216

Email: [jan.hauser@us.pwc.com](mailto:jan.hauser@us.pwc.com)

**Douglas Parker**

Partner

Phone: 1-973-236-4707

Email: [douglas.t.parker@us.pwc.com](mailto:douglas.t.parker@us.pwc.com)

**Angela Fergason**

Director

Phone: 1-408-817-1216

Email: [angela.fergason@us.pwc.com](mailto:angela.fergason@us.pwc.com)

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