THE OHIO SOCIETY OF CPAs

May 14, 2014
Youngstown State University

YSU CPE Day

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Hill, Barth & King L.L.C.

Big GAAP, Little GAAP – Who Gives a GAAP?

Session #010

Upcoming Events

NOTICE TO READERS:

These course materials have been prepared solely for continuing education purposes. Since the subject matter has not been considered and acted upon by senior technical committees of The Ohio Society of CPAs, it does not represent an official position of the Society

Accounting & Auditing Update 2014

Topics

- Professional Issues Update
- New COSO Framework
- Newly Effective GAAP
- Auditing Standards "Mini" Update
- SSARS (Review & Compilation) Update
- PCC New Proposals, FRF for SME's

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Professional Issues Update

Including Ethics

AICPA Center For Plain English Accounting

- "National Office" for smaller firms- PCPS effort- subscription
- **Full Access Version –**(Limited access version also available)
  - Practical, monthly reports and news and alerts on current A&A topics and guidance
  - Access to the website and database with past reports and information to conduct your own research
  - Eight two-hour NASBA certified webinars for one person (each additional participant may attend for $25 per webinar)
  - Written responses to submitted written questions on various A&A topics, standards, guidance, etc.

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New AICPA Accounting and Valuation Guide

"Testing Goodwill for Impairment"

Contains:

- Practice issues
- Examples
- Disclosures

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SEC Crowdfunding Rules

To be finalized in early 2014

- Businesses must only use one portal at a time
- Variety of legal paperwork to be filed
- $1MM limit on funding from non-accredited investors
- Business raising more than $100,000 need reviewed financial statements
- Audit required if more than $500,000 raised

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ERISA Audits

- DOL cracking down on “dabblers”- firms who audit less than 5 plans
- According to DOL firms belonging to AICPA ERISA Audit Quality Centers do better quality work
- DOL asking Congress for more authority to sanction firms doing substandard work
- DOL to conduct Audit Quality Study in 2014

Noted Deficiencies In ERISA Audits

Auditors giving too much credence to:

- SOC 1 reports- need to inspect reports and test inputs
- Work performed by actuaries
- Work performed by appraisers on ESOPS
- Predecessor auditor work

Ethics

Interpretation 101-3 Non-Attest Services

Provides guidance on cumulative effect on independence when providing multiple non attest services

CPA must evaluate whether performance of in the aggregate these services create threat to independence by application of safeguards

Effective for engagements covering periods beginning on or after December 15, 2014

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Refresher- Non Attest Services

Some examples:

-Cash to accrual conversion

-Preparing financial statements

CPA may not assume management responsibilities

CPA firm communication about accounting principles etc is not a non attest service if done as part of audit, review or compilation

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101-18—Application of the Independence Rules to Affiliates

Financial interests in, and other relationships with, entities that are related in various ways to a financial statement attest client may impair independence. This interpretation provides guidance on which entities should be considered an affiliate of a financial statement attest client and subject to the independence provisions of the AICPA Code of Professional Conduct.

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Ethics ED- Those Charged With Governance

- Proposed definition in Code of Professional Conduct for the phrase “those charged with governance”
- This phrase appears in Code of Professional Conduct and other places in professional literature
- Would be similar to definition in Auditing Standards

Ethics Codification- New Code of Conduct

- Primary goal- restructure so members and others can apply the rules and reach correct conclusions
- Two conceptual frameworks- one for those in practice and one for those in business
- Term client replaced by “attest client”
- Ethical conflict resolution
- False, misleading acts- applied to all members

Ethics-Codification

- Would be consistent with IESBA Code
- Comments due 1/27/2014
- Would require member to take reasonable steps to identify circumstances that might create conflict of interest
- No change to existing rules

Threats and Safeguards Approach

Also known as the "conceptual framework approach" is a way of identifying, evaluating, and addressing threats to compliance with the rules resulting from a specific relationship or circumstance.

Members are required to use the threats and safeguards approach only when there is no guidance on point.

Independence of Appearance

- Possibility that convivial working relationship with attest client personnel might give impression that CPA is "too close' to client
- Watch emails- if exchanges are too frequent, less than professional in tone- coarse language
- Acceptance of gifts and entertainment- should be firm policy
- Discuss independence in planning stage

The New COSO Document

COSO *Internal Control-Integrated Framework*

- Committee of Sponsoring Organizations (COSO) is comprised of the AICPA, FEI, IMA,IAA and AAA representatives
- Original COSO document "Internal Control-Integrated Framework" dates to 1992
- Updated in May, 2013 to incorporate changes that have occurred in the business and operating environment
- Old version will be replaced by this one on December 15, 2014

New COSO Document

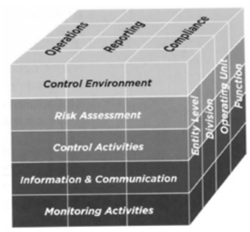
- Applicable to all entities- business, NPOs and Government
- ASB considering changes to AU-C 315 *Understanding the Entity* to incorporate new wording
- May or may not not result in significant changes to required audit procedures
- Clients should be made aware of document

What Has Not Changed

Core definition of Internal Control:

Internal Control is a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting and compliance.

Relationship of Objectives and Components



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Overview of What Has Changed (Appendix F)

- Applies a principles based approach
- Clarifies requirements for effective internal control
- Expands the reporting category of objectives
- Clarifies the role of objective-setting in internal control
- Considers globalization of markets and operations

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What has Changed

- Enhances governance controls
- Considers different business models and organizational structures
- Considers demands and complexities in laws, rules and regulations and standards
- Considers expectations for competencies and accountabilities
- Reflects increased relevance of technology
- Enhances consideration of anti-fraud expectations

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3 Key Changes

- **Articulating the role of a company when outsourcing.** While today's businesses can outsource many activities, they can *never* outsource responsibility.
- **Putting fraud right out in the forefront.** A business's control structure must now address issues of fraud directly.
- **Highlighting the critical nature of IT.** Information technology is a needed component that cannot be avoided in today's business environment.

If Internal Control is Effective..

There is reasonable assurance that the organization:

- Achieves effective and efficient operations
- Understands the extent to which operations are managed effectively and efficiently when external events may have a significant impact
- Prepares reports in conformity with regulations, etc
- Complies with applicable laws etc

Limitations on Internal Control

May result from:

- Suitability of objectives established
- Human judgment in decision making
- Human failures- simple errors
- Ability of management to override controls
- Collusion
- External events

Update articulates 17 principles of effective internal control

Control Environment	1. Demonstrates commitment to integrity and ethical values 2. Exercises oversight responsibility 3. Establishes structure, authority and responsibility 4. Demonstrates commitment to competence 5. Enforces accountability
Risk Assessment	6. Specifies suitable objectives 7. Identifies and analyzes risk 8. Assesses fraud risk 9. Identifies and analyzes significant change
Control Activities	10. Selects and develops control activities 11. Selects and develops general controls over technology 12. Deploys through policies and procedures
Information & Communication	13. Uses relevant information 14. Communicates internally 15. Communicates externally
Monitoring Activities	16. Conducts ongoing and/or separate evaluations 17. Evaluates and communicates deficiencies

Organization of Document

- Separate chapter for each element
- Each principle has "points of focus"
- Each "point of focus" has an explanation and guidance

Control Environment

Control environment is the set of standards, processes and structures that provide the basis for carrying out internal control across the organization

5 Related Principles…..

Control Environment- Principle 1

The organization demonstrates a commitment to integrity and ethical values by

- Establishing standards of conduct
- Leading by example in these matters- **tone at the top**
- Evaluating management and other personnel, outsourced providers, and business partners for adherence to standards of conduct
- Developing processes to report and promptly act on deviations

Control Environment- Principle 2

Board of Directors demonstrates independence from management and exercises oversight for the development and performance of internal control by:

- Establishing the roles, responsibilities and delegation of authority of Board of Directors
- Establishing policies and practices for meetings between Board and management

Control Environment- Principle 2

- Identifying and reviewing board candidates
- Reviewing management's assertions and judgments
- Obtaining an external view
- Considering whistle-blower information about financial statement errors and irregularities

Whistle Blower Approach

Approach: **Considering Whistle-Blower Information about Financial Statement Errors and Irregularities**

The audit committee considers information obtained from the company's whistle-blower and anti-fraud programs (or similar processes) to monitor the risks in misstatements in financial reporting. These may include risks of inappropriate acts by staff and management override of controls. The audit committee reviews any whistle-blower allegations and evaluates management's analysis of significant matters, potential impact on financial reporting, and corrective actions being taken.

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Control Environment- Principle 3

Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives by

- Defining roles and reporting lines and assessing them for relevance
- Defining authority at different levels of mgmt
- Maintaining job descriptions and service level agreements
- Defining role of internal auditors

Control Environment- Principle 4

Organization demonstrates commitment to attract, develop, and retain competent individuals in alignment with objectives by:

- Establishing required knowledge, skills and expertise
- Linking competence standards to established policies and practices in hiring, training, retention decisions

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Control Environment-Principle 5

The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives by:

- Defining and confirming responsibilities
- Developing balance performance measures, incentives and rewards
- Evaluating performance measures for intended influence
- Linking compensation and other rewards to performance

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Risk Assessment

Risk is defined as the possibility that an event will occur and adversely affect the achievement of objectives.

Risk assessment involves a dynamic and iterative process for identifying and assessing those risks.

Risks are considered relative to established tolerances

4 Related Principles…

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Risk Assessment- Principle 8

The organization considers the potential for fraud in assessing risks to the achievement of objectives by:

- Conducting fraud risk assessments
- Considering approaches to circumvent or override controls
- Considering fraud risk in internal audit plan
- Reviewing incentives and pressures related to compensation arrangements

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Sample Approaches

Risk Assessment | Assesses Fraud Risk

Approaches and Examples for Applying the Principle

Approach: **Conducting Fraud Risk Assessments**

Management conducts a comprehensive fraud risk assessment to identify the various ways that fraud and misconduct can occur, considering:

- The degree of estimates and judgments in external financial reporting
- Methodology for recording and calculating certain accounts (e.g., inventory)
- Fraud schemes and scenarios that are common to the industry sectors and markets in which the entity operates
- Geographic regions where the entity does business
- Incentives that may motivate fraudulent behavior
- Nature of automation
- Unusual or complex transactions subject to significant management influence
- Last-minute transactions
- Vulnerability to management override and potential schemes to circumvent existing control activities

From these considerations, management makes an informed assessment of specific areas where fraud might exist and the likelihood of their occurrence and potential impact.

- Considers Various Types of Fraud
- Assesses Incentive and Pressures
- Assesses Opportunities
- Assesses Attitudes and Rationalizations

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Example

Example: **Assessing Fraud Risk**

David Kates, the chief compliance officer at a global retail operation, annually conducts a fraud risk assessment. In doing so, he interviews management at all the international locations about fraud issues. He analyzes:

- Historical fraud activities, including theft of inventory and the processes in place to identify and record such theft
- The methodology used for recording and calculating inventory and shrinkage
- Whistle-blower reports
- The number of manual entries versus automated entries recorded
- The number of late entries due to subjective estimates

With this information, Mr. Kates forms a preliminary view of the potential fraud activities, which he discusses with management of each jurisdiction in order to consider implications and what control activities can reduce the risk of fraud. He also has discussions with human resources personnel and reviews information in the staff files. He uses his historical knowledge and staff information to assess the attitude of the local management toward the tolerance of fraud and to determine whether local management may rationalize fraudulent activities, including corruption.

After completing his fraud risk assessment, Mr. Kates submits a report to the audit committee for its consideration in management oversight.

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Control Activities

Control activities are the actions established through policies and procedures that help ensure that management’s directives to mitigate risks to the achievement of objectives are carried out.

3 Related Principles…

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Control Activities- Principal 10

- Considering types of control activities
- Considering alternative control activities to the segregation of duties
- Identifying incompatible functions

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Example- Segregation of Duties

Example: **Using Alternative Control Activities when Access to Purchasing Transactions Are Not Segregated**[18]

Luther Optical is a multi-million-dollar designer, manufacturer, and distributor of consumer and industrial optical products. There are two staff members in the purchasing department, each of whom is authorized to prepare, authorize, and issue purchase orders up to $5,000. Because no one reviews these purchase orders before they are sent to vendors, there is a risk that unintentional errors or intentional fraudulent acts will result in inventory valuation errors, obsolescence, or shortages due to diverted shipments. To reduce this risk to an acceptable level, management relies on a combination of control activities carried out by other staff members. These include, but are not limited to, the following:

- An inventory clerk documents and tracks all inventory levels, reducing the risk of obsolescence.
- An inventory receiving clerk evaluates, documents, and reports to management unusual inventory movement, such as excessive ordering that could lead to obsolescence.
- A payables clerk matches invoices to purchase orders and receiving reports before amounts are paid, reducing the risk of errors resulting from diverted shipments.
- A controller reviews exception reports of all inventory purchases with a price more than 10% above current average costing.

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Information and Communication

- Information is necessary for the entity to carry out internal control responsibilities to support the achievement of its objectives.
- Communication is the continual, iterative process of providing, sharing and obtaining necessary information
- Communication is both internal and external

3 Related Principles…

Monitoring

Ongoing evaluations are used to ascertain whether each of the five components of internal control is present and functioning

2 Related Principles…

Example- Monitoring Activities- Principle 16

- Designing and implementing a dashboard
- Using technology to support monitoring activities
- Conducting separate evaluations
- Using internal audit to conduct separate evaluations
- Using controls at an outsourced service provider

Approach-Using Metrics

Approach: **Identifying and Using Metrics**[23]

Management identifies metrics that correlate to the completeness and accuracy of financial transactions to provide ongoing evaluations of established control activities. When identifying metrics, management considers the processes and sub-processes that should be monitored, and develops the appropriate measure and frequency for the evaluation.

The metrics may use the following information:

- Historical performance data, which may be useful for comparisons to current performance data
- Expected performance targets, which may be used to benchmark current performance against expected performance

Some metrics have clearly defined allowable tolerances that have been calculated for current performance data, which may be used to highlight anomalies. Other metrics have less defined thresholds and are reviewed by knowledgeable employees for reasonableness and unusual items.

Example- Using Metrics

Example: **Using Metrics to Monitor Payroll**

Approximately 90% of Mynarski Manufacturing employees are located at company plant sites. To monitor whether the payroll processing control activities are working, Henrik Saunders, the corporate payroll manager, reviews the plant payroll metrics. Payroll metrics include:

- Current head count compared with expected and historical head count for the month, quarter, and year
- Current payroll compared with expected and historical payroll for the month, quarter, and year
- Current overtime in hours and dollars compared with expected and historical overtime in hours and dollars for the month, quarter, and year

In his review, Mr. Saunders looks for any unusual fluctuations, such as increases and decreases in the number of employees and excessive overtime. His review is done in the context of current plant productivity and target thresholds based on historical data and planned productivity, which varies by season. If Mr. Saunders identifies any fluctuations, he investigates the underlying reasons and adjusts the process or control activities as needed.

Newly Effective GAAP

ASU 2014-02 and 03

- PCC projects on goodwill and interest rate swaps
- Finalized by FASB
- Covered in private company section

ASU 2014-01 Accounting for Investments in Qualified Affordable Housing Projects

- Provides guidance on accounting for investments by a reporting entity in flow-through limited liability entities that manage or invest in affordable housing projects that qualify for the low-income housing tax credit.
- Permits reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met

ASU 2014-01 Accounting for Investments in Qualified Affordable Housing Projects

- Effective for public entities for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014. For all entities other than public entities- effective for annual periods beginning after December 15, 2014, and interim periods within annual reporting periods beginning after December 15, 2015. Early adoption is permitted.
- Retroactive application

ASU 2013-12 Definition of A Public Business Entity

- Defines what constitutes a public business entity to distinguish between different types of entities for standard-setting purposes and on determining which companies are to be excluded from the scope of the Private Company Decision-Making Framework.
- Definition for Master Glossary
- Will not affect existing standards

Entity is Public IF:

a) It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
b) It is required by the Securities Exchange Act of 1934, as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency, other than the SEC.

Entity is Public IF

c) It is required to file or furnish financial statements with a regulatory agency (foreign or domestic) in preparation for the sale of securities or for purposes of issuing securities.
d) It has (or is a conduit bond obligor for) securities that are traded, quoted, or listed on an exchange or an over-the-counter market

Entity is Public IF

e) It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including footnotes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

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An Entity is Public If

An entity may meet the definition of a public business entity solely because its financial statements or financial information is included in another entity's filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC.

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ASU 2013-11 Income Taxes-Presentation of an Unrecognized Tax Benefit when a net operating loss carryforward, a similar tax loss or a tax credit carryforward exists

Effective- public after 12/15/2013, private 12/15/2014- early adoption permitted

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ASU 2013-09 Deferral of the Effective Date of Certain Disclosures for Nonpublic Employee Benefit Plans in Update No. 2011-04

Effective immediately (7/18/2013) for financial statements that have not been issued

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ASU 2013-08 Investment Companies: Amendments to the Scope, Measurement, and Disclosure Requirements

Effective prospectively for fiscal years beginning after December 31, 2013. Early application prohibited

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ASU 2013-07 Presentation of Financial Statements (Topic 205) Liquidation Basis of Accounting

Effective prospectively for fiscal years beginning after June 15, 2014. Early adoption permitted

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ASU 2013-06 Not-for-Profit Entities (Topic 958) Services Received from Personnel of an Affiliate

Effective prospectively for fiscal years beginning after June 15, 2014. Early adoption permitted

ASU 2013-06: Not-for-Profit Entities; Services Received from Personnel of an Affiliate (Continued)

- Affects NFP receiving services from personnel of an affiliate that are not charged for the services
- Recognize services at:
  - Cost recognized by the affiliate, or
  - Fair value of the service
- Do not report services as contra expense or asset
- Special rules for health care NFP regarding change in Net Assets

ASU 2012-05 Statement of Cash Flows (Topic 230) Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows

Effective prospectively for fiscal years and interim periods within those years, beginning after June 15, 2013. Retrospective application and early adoption permitted

ASU 2012-05: Not for Profit Cash Flow Issues

- Standard provides guidance on classification on cash inflows on the sale of donated assets
- Generally, cash flows from such sales are classified as **investing** cash flows
- Assets donated with restrictions that are sold shall be classified as **financing** activities
- Assets that were donated without restrictions that are sold nearly immediately are classified as **operating** activities

ASU 2013-02 Comprehensive Income (Topic 220) Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income

An entity is required to apply the amendments for reporting periods including interim periods beginning after December 15, 2012 for public companies and are effective for reporting periods beginning after December 15,2013 for private companies

Proposed GAAP

Revenue Recognition

Final Expected 1st Half 2014

Proposed Jt. Rev Rec Model

1. Identifying the contract
2. Identifying the performance obligations
3. Determining the transaction price
4. Allocating the transaction price to performance obligation
5. Recognizing revenue

Note: For contractors change orders would now be contract modifications.

1. Contract with a customer

- Contract – rights and obligations – penalty for non-performance
- Collectability – reasonably assured
- Performance obligations – enforceable promise (implicit or explicit) in contract with customer to transfer goods/services
- Price
  - Combine contracts – if prices are interdependent
  - Separate contracts – if prices are independent

Contract Modifications

- Only combine contracts when (one or more of the following exists):
  - The contracts were negotiated as a package
  - The fee in one contract depends upon the other
  - Some or all of the goods or services in one contract would be combined with some or all of the goods or services in the other into a single performance obligation

  Note: There is never an impact to performance obligations that were fully satisfied.

2. Performance obligation

- Enforceable promise (implicit or explicit) in contract with customer to transfer goods/services
- Split the sales and after-sales service
  - Auto – 30K or 3 yr warranty – need to recognize deferred revenue for the service
  - Every time customer brings the car in for service recognize revenue and cost of servicing car
- Similar to "multiple deliverable" term currently used

Performance Obligations

- Goods/services transferred continuously
- Acceptable methods
  - Output methods (units produced/delivered)
  - Input methods (costs/hours incurred)
  - Methods based on passage of time

3. Determine transaction price

- Measure at amount of consideration to which entity is entitled
- Allocate in proportion to stand-alone selling price
- Best evidence is observable price when sold separately
- Must consider the effects
  - Time value of money if significant financing component
  - Non-cash consideration
  - Consideration payable to the customer

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Determine transaction price

Customer Right of Return - Refunds

- Current US GAAP: returns are estimated based on historical experience, with an allowance recorded against sales.
- Proposed guidance: revenue is not recognized for goods expected to be returned, rather a liability is recognized for the expected amount of refunds to customers using a probability-weighted approach.
- An asset and adjustment to COGS is recognized for the right to recover goods.
- The asset is adjusted for any impairment, if necessary.

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4. Allocate transaction price

- Allocate selling price based on the performance obligation FV of components

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5. Recognize revenue

- Recognize revenue when a performance obligation is satisfied
  - Customer obtains control of goods/services
  - Control defined as ability to direct the use and receive benefit from goods/services
- Indicators of control
  - Unconditional obligation to pay
  - Legal title
  - Physical possession

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Disclosures

- Qualitative and quantitative info about
  - Contracts with customers
  - Significant judgments and changes in judgment
  - Rights to consideration
- Customer contracts
  - Disclose revenue into categories that best depict contract types (geography or type of customer)
  - Tabular reconciliation of contract assets and liabilities

  Some disclosure relief for private companies

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Transition

- Full retrospective application to all prior periods- but some practical expedients
- Cost is expected to significantly impact some entities
- Effective date for public companies- annual reporting periods beginning on or after 1/1/16 and private companies for annual reporting period beginning after 12/15/2017

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Leases

WHO KNOWS?????

Financial Instruments Projects

Two Parts to Project thus far

- Classification and Measurement
- Impairment

Hedging part on hold

Joint with IASB

Final expected 1st half 2014

Going Concern ED

Evaluate at each annual and interim reporting period and start providing footnote disclosures when it is either

(1) *more likely than not* that the entity will be unable to meet its obligations within 12 months after the financial statement date without taking actions outside the ordinary course of business or

(2) *known or probable* that the entity will be unable to meet its obligations within 24 months after the financial statement date without taking actions outside the ordinary course of business.

Going Concern ED- When threshold is met- disclose:

- (1) the principal conditions and events that give rise to the entity's potential inability to meet its obligations,
- (2) the possible effects those conditions and events could have on the entity,
- (3) management's evaluation of the significance of those conditions and events, (4) mitigating conditions and events

Going Concern Proposed Disclosures

(5) management's plans that are intended to address the entity's potential inability to meet its obligations.

An entity that is an SEC filer is required to evaluate whether there is substantial doubt about its going concern presumption. If there is substantial doubt, the entity would disclose that determination in the footnotes.

Going Concern-Non SEC Filer

An entity that is not an SEC filer would not be required to evaluate or disclose whether there is substantial doubt about its going concern presumption but would be required to apply all of the other disclosure requirements within

No release date at this time

Development Stage Entities- ED

- Would supersede all of the incremental presentation and disclosure requirements for development stage entities that are currently required by Topic 915, Development Stage Entities.
- Potential additional disclosures
- Would be applicable to financial statements issued after the effective date, with the option of early adoption
- Still in comment period

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Discontinued Operations- Convergence

- Objective of the project is to improve the definition and reporting of discontinued operations.
- Some stakeholders have said that too many disposals of assets qualify for discontinued operations presentation.
- Results in financial statements that are not decision useful for users and in higher costs for preparers.
- Expected 1st Qtr 2014

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Discontinued Operations- ED

Results of operations of a *component of an entity* or a group of components of an entity would be reported in discontinued operations if both of the following criteria are met:

- The component or group of components has been disposed of, or is classified as held for sale, together as a group in a single transaction
- The disposal of the component or group of components represents a strategic shift that has (or will have) a major effect on an entity's financial results.

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Technical Corrections and Improvements- ED

Minor changes to codification

Final expected 1st Qtr 2014

Disclosure Framework

- Objective is to improve the effectiveness of disclosures in notes to financial statements by clearly communicating the information that is most important to users of each entity's financial statements.
- Two parts- Board's Decision Process and Entity's Decision Process
- Two Eds expected 1st Qtr 2014

Investment Companies: Disclosures about Investments in Another Investment Company

- Would require disclosures in an investment company's financial statements that will provide transparency into the risks, returns, and expenses of an investee that is also an investment company.
- The disclosures would be required for
  - -Investments in unconsolidated investment companies.
  - -The first level of investments in another investment company, not to the second or third level of investments.

ED expected 1st QTR 2013

EITF Projects

Project	4 Q	1st
Accounting for Service Concession Arrangements (12-H)	F	
Accounting for Investments in Tax Credits (13-B)	F	
Reclassification of Collateralized Mortgage Loans upon a Troubled Debt Restructuring (13-E)	F	
Accounting for Share-Based Payments When the Terms of an Award Allow a Performance Target to Be Achieved After the Requisite Service Period (13-D) (Exposure Document issued 10/23/13)	C	
Accounting for the Effect of a Federal Housing Administration Guarantee (13-F)	E	
Determining Whether the Host Contract in a Hybrid Financial Instrument Is More Akin to Debt or to Equity (13-G)	C	
Measuring the Financial Liabilities of a Consolidated Collateralized Financing Entity (12-G)		F
Recognition of New Accounting Basis (Pushdown) in Certain Circumstances (12-F)		

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Audit Standards

Technical Practice Aids

- TIS 8800.42- Component Audit Report of Balance Sheet Only- opinion on group consolidated financial statement may not make reference to balance sheet only report. Group engagement team has to perform procedures on financial information of component

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TIS 8800.43- Using another accounting firm to observe inventory

When observation of inventory at remote location outsourced to another auditor, other auditor not considered component auditor

TIS 9100.08 Audit Firm with multiples addresses on letterhead

Report needs to indicate city and state where the auditor practices

Audit Reminders

Peer Review Findings- Accounting

- Disclosures of open tax years
- Fair Value disclosures by levels 1, 2 and 3
- Disclosure of 5 year debt maturities
- Risks and uncertainties- use of estimates and concentrations
- Disclosure of date through which subsequent events have been evaluated

Peer Review Findings- Audit

- Failure to document communication with those charged with governance
- Incomplete documentation of planning and supervision related to risk
- Failure to communicate internal control matters identified in audit
- Failure to document expectations for analytical procedures and compare results

Peer Review Findings- Audit

- Sampling- failure to document sample size determination, methodology, failure to project results to population
- Governmental and NFPs- failure to use risk based approach to determine major programs, missed major programs

SSARS Update

Findings in Peer Review- Compilations

- Basic presentation requirements- wrong periods, captions and descriptions
- Failure to appropriately title fs or describe basis
- Basic report elements missing
- Issuing tax basis financial statements and report not modified for this

Findings in Peer Reviews- Reviews

- Failure to document expectations when performing analytical review
- Management representations- letter failed to include all periods; letter did not include statement about management's responsibility to detect and prevent fraud
- Basic reporting requirements
- Errors in engagement letter
- Reporting on comparative fs and supplement info

Compilation and Review Engagements (AICPA CAR Guide)

- Updated in March 2013.
- Developed under the supervision and authority of ARSC, and is considered an interpretive publication pursuant to AR 60.18.
- Purpose of the Guide is to assist accountants in compiling or reviewing financial statements in accordance with the SSARSs.

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Nonauthoritative Exhibits

- Exhibit A, *Analytical Procedures in a Review Engagement*- illustrates how an accountant might document expectations in a review engagement.
- Exhibit B, *Going Concern Considerations*- provides accounting guidance with respect to an entity's ability to continue as a going concern.

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SSARS No. 20- Exception to scope of SSARS 19

Applies to reviews of nonissuers' interim financial information when **all** of the following conditions are met:

a. The entity's latest annual financial statements have been audited by the accountant or a predecessor.
b. The accountant either has been engaged to audit the entity's current year financial statements, or when it is expected that the current year financial statements will be audited, the appointment of another accountant to audit the current year financial statements is not effective prior to the period covered by the review.
c. The entity prepares its interim financial information using the same financial reporting framework as that used to prepare its annual financial statements.

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Economic Consideration that May Affect Comp and Review Engagements

- *Fair Value Measurements and Disclosures.* Since the economic contraction is likely to cause many companies to consider the need for fair value measurements, see FASB ASC 820
- *Accounting Considerations.* The economic contraction is likely to affect the measurement, presentation, and related disclosures for certain assets, liabilities, and expenses of small and midsize nonpublic companies in preparing their financial statements in conformity with generally accepted accounting principles.
- *Liquidation of the Company.* If the impact of the recession is so severe that a company cannot survive, liquidation may occur.
- *Disclosure Considerations.* Certain disclosures that are not necessarily related to measurements and presentation in the financial statements: the ability of the company to continue as a going concern; disclosure of subsequent events; and disclosure of commitments, contingencies, risks, and uncertainties may also be needed.

ARSC Exposure Draft

- *Preparation of Financial Statements*
- *Compilation Engagements*
- *Association With Financial Statements*

Would be effective for periods ending on or after 12/15/15- early adoption permitted

Drafting in Accordance with ARSC's Clarity Drafting Conventions

- Objectives
- Definitions
- Separating requirements from applications
- Numbering- applications have A prefix
- Formatting to enhance readability

Proposed SSARS *Preparation of Financial Statements:*

Would provide requirements and guidance when an accountant is engaged to prepare financial statements for an entity but has not been engaged to perform a compilation, review, or audit with respect to those financial statements.

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Proposed SSARS *Compilation Engagements*

Would provide requirements and guidance that would apply only when an accountant is engaged to perform a compilation of historical financial statements.

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Proposed Standards

Compilation of Financial Statements

Clarifies that a compilation only exists if the accountant is actually engaged to compile the financial statements

Adds requirements for a written and signed acknowledgment from management over their responsibilities **(engagement letter)**

Modifies the report to be consistent with the report format in the auditing standards **(headers & city, state)**

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Proposed SSARS *Compilation Engagements*

Special considerations

Clarifies reporting requirements when financial statements use a special purpose framework (previously referred to as OCBOA)

Clarifies reporting requirements when departures exist

Clarifies reporting requirements when there is subsequent discovery of facts and the report is reissued

Clarifies disclosure requirements needed to be able to issue a report

Proposed SSARS *Association With Financial Statements*

Would provide requirements and guidance when an accountant agrees to permit the use of the accountant's name in a report, document, or written communication that includes financial statements with respect to which the accountant did not issue a compilation, review, or audit report.

Proposed SSARS *Association With Financial Statements*

Defines associated with financial statements

Defines accountant's responsibilities

Defines client's responsibilities

Provides a reporting option for the accountant

- Moving from "Prepare and Submit" to "Reporting"
- May add a statement: "These FS have not been compiled, reviewed or audited."

Effective Date

- The effective date for the proposed standards is expected to be for periods ending on or after Dec. 15, 2014.

Private Company Financial Reporting

AICPA Financial Reporting Framework for SMEs

AICPA Financial Reporting Framework for Small and Medium Sized Entities

- Self contained special purpose framework
- Mix of traditional methods and accrual income tax basis
- Could be used where GAAP reporting not required- "Main Street" businesses
- Non-authoritative
- Financial statements audited, reviewed, compiled as an OCBOA

What is a SME?

- Entity is not required to prepare GAAP FS
- Entity has no plans to go public
- Is a for profit entity
- Owner is also the person who runs entity
- No highly specialized industry guidance
- No complex transactions
- No foreign activities
- Users have access to management

AICPA FR FW for SME

- Uses historical cost as its measurement basis
- No complicated fair value measurements.
- Does not require complicated accounting for derivatives, hedging activities, or stock comp
- Disclosure requirements are targeted, providing users of financial statements with the relevant information they need while recognizing that those users can obtain additional information from management if they desire.

AICPA FR FW for SME

- Can be downloaded

http://www.aicpa.org/InterestAreas/FRC/AccountingFinancialReporting/PCFR/DownloadableDocuments/FRF-SME/FRF-SMEs-Framework.PDF

- Has sample financial statements and disclosures
- AICPA is promoting with ads targeted to users and an email campaign

Significant Differences from GAAP

- Taxes- can use taxes payable method or deferred income taxes method
- Goodwill- amortize over 15 years or
- VIEs- doesn't require primary beneficiary to consolidate
- Leases- if lease transfers substantially all benefits and risks of ownership to lessee, than capitalize

Significant Differences From GAAP

- Asset Impairment- reduce inventory to carrying value- other assets not addressed
- Debt and Equity Investments- recurring adjustments of carrying amount of investments held for sale- changes recognized in net income. If not held for sale, record at historical cost

Training Tools

- In firm training tools include videos, flyers, power point presentations and a toolkit
- Client facing tools include videos, articles, FAQs, checklists, social media blurbs

All available on AICPA website

OCBOA Practice Aids

- Now called "special purpose framework"
- Cash and tax basis not precluded by new FRF for SME
- New practice aid *Accounting and Financial Reporting Guidelines for Cash and Tax Basis Financial Statements*
- Also separate practice aid for OCBOA in State and Local Government Financial Statements

FASB Private Company Council

FASB Private Company Council

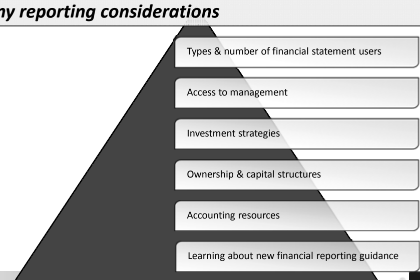
- 10 members- all with private company experience as auditor, user, preparer
- PCC reviews and proposes alternatives within U.S. GAAP to address the needs of users of private company financial statements.
- The PCC also serves as the primary advisory body to the FASB on the appropriate treatment for private companies for items under active consideration on the FASB's technical agenda.

FASB Private Company Decision Making Framework

- Outlines criteria to determine whether and in what circumstances it is appropriate to adjust financial reporting requirements for private companies following U.S. Generally Accepted Accounting Principles (GAAP)
- Finalized in July 2013 by PCC
- Finalized by FASB December 2013

Differential Factors

***Six* significant factors that most differentiate private / public company reporting considerations**



Framework Structure

Five modules

- Recognition and Measurement (R&M)
- Display (Presentation)
- Disclosures
- Effective Date
- Transition Method

- *2-5 pages per module, flowcharts where appropriate*
- *Modules include background, summary & basis for recommendations*

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*ASU **2014-02-Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps- Simplified Hedge Accounting Approach***

Private companies have alternative to account for "plain vanilla" interest rate swaps – measure designated swap at settlement value instead of fv

Criteria

- Both rate on swap and borrowing based on same index and reset period
- Terms of swap are typical plain vanilla
- Repricing and settlement dates for swap and borrowing match or differ by no more than a few days

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ASU 2014-02 Interest Rate Swaps

- Swap's fv at time of inception is at or near zero
- Notational amount of swap is equal to or less than principal amount of borrowing
- Term of swap is equal to or less than term of borrowing
- Hedge documentation completed up until date on which annual fs available to be issued
- Can elect to apply to existing swaps if meets criteria
- Effective years beginning after 12/15/2014- early adoption permitted

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ASU 2014-03-*Accounting for Goodwill*

- Private company can make election to amortize goodwill over 10 years or less than 10 years if entity can demonstrate another useful life
- Can make election to perform impairment testing at entity level or reporting unit level.
- Test for impairment only when triggering event occurs that may reduce fv of entity below its carrying amount- can use qualitative test
- No new disclosures and no tabular rollforward

ASU 2014-03- *Accounting for Goodwill*

- Effective prospectively for GW existing at beginning of period of adoption and for GW generated from business combinations entered into during fiscal years beginning after 12/14/2014- early adoption permitted
- FASB considering this for public companies as well

PCC Pending -*Applying Variable Interest Entity Guidance to Common Control Leasing Arrangements*

Applies when:

- Private co and lessor are under common control
- Two entities have a leasing arrangement with each other
- Substantially all activities related to both of these entities are either related to leasing or its support
- Liabilities of lessor entity only finance assets leased to operating company and are not collateralized by assets of operating company

PCC Pending- Applying VIE Guidance to Common Control Leasing Arrangements-Disclosures

- Key terms of leasing arrangements
- Amount of debt and/or significant liabilities of lessor entity
- Key terms of existing debt agreements of lessor entity
- Key terms of any other explicit interest related to lessor entity under common control
- Disclosure requirements under other applicable U.S. GAAP (for example, Topics 460, 840, and 850, Related Party Disclosures) about the lessor entity.
- Disclosures could be made by aggregating all disclosures into a single note or by including cross-references within the notes to the financial statement.

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PCC Pending-Applying VIE Guidance to Common Control Leasing Arrangements

- Must be applied to all like leasing arrangements
- Effective for the first annual period beginning after December 15, 2014, and interim and annual periods thereafter. Early application is permitted

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PCC Pending- *Accounting for Identifiable Assets in a Business Combination*

- A private company could elect to recognize only those intangible assets arising from noncancellable contractual terms or those arising from other legal rights. Otherwise, an intangible asset would not be recognized separately from goodwill even if it is separable.
- FV of intangible assets arising from noncancellable contract terms should be measured on the basis of the contract's remaining noncancellable term regardless of whether market participants would consider potential contractual renewals in determining fair value.

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PCC Pending-Accounting for Identifiable Assets in a Business Combination

- FV of intangible assets that arise from other legal rights that are noncontractual (for example, a registered trade name) should continue to be recognized at fair value in accordance with Topic 820, Fair Value Measurement, incorporating all expectations of market participants about such intangible assets.
- Status- staff to do more research- stay tuned