

# Insights

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## Accounting

### Conforming Amendments Resulting from Statement No. 158

FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, amended the recognition provisions of Statement No. 87, *Employers' Accounting for Pensions*, Statement No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits*, and Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*, to require recognition of the funded status of defined benefit postretirement plans in an employer's balance sheet. However, Statement No. 158 did not amend the illustrations contained in Appendix B of Statement No. 87, Appendix B of Statement No. 88, or Appendix C of Statement No. 106; nor did it amend the questions and answers contained in the FASB Special Reports related to those Statements. Therefore, the Financial Accounting Standards Board has issued FASB Staff Position (FSP) No. FAS 158-1 to provide conforming amendments to these illustrations and Special Reports. The FSP also incorporates the questions and answers contained in the Special Reports into the respective Statements as appendices. The FSP therefore supersedes the FASB Special Reports related to Statements No. 87, 88 and 106.

The conforming amendments made by this proposed FSP are effective as of the effective dates of Statement No. 158. The unaffected guidance that this FSP codifies into Statements No. 87, 88, and 106 does not contain new requirements and therefore does not require a separate effective date or transition method. The FSP is available in full at [http://www.fasb.org/fasb\\_staff\\_positions/fsp\\_fas158-1.pdf](http://www.fasb.org/fasb_staff_positions/fsp_fas158-1.pdf).

### TPAs Released Regarding the Application of SOP 05-1

The Accounting Standards Team of the American Institute of Certified Public Accountants (AICPA) has released 11 Technical Practice Aids (TPAs) relating to the application of AICPA Statement of Position (SOP) 05-1, *Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts*. SOP 05-1 provides guidance on accounting by insurance enterprises for deferred acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards No. 97, *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*. The SOP defines an internal replacement as a modification in product benefits, features, rights, or coverages that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. The recent TPAs address a variety of issues, including the following:

- TPA 6300.25, *Integrated/Nonintegrated Contract Features in Applying SOP 05-1*. This TPA concludes that contract features that do not meet the definition of "nonintegrated" contract features

need to be evaluated to determine if the contract modification results in a substantially changed replacement contract in accordance with the criteria in SOP 05-1.

- TPA 6300.26, *Evaluation of Significance of Modification in Applying SOP 05-1*. This TPA concludes that in assessing the significance of change in the degree of mortality risk, morbidity risk, or other insurance risk, the insurance enterprise should consider the specific facts and circumstances of the modification as well as which approach or multiple approaches it considers most appropriate in analyzing the substance of the change. The approach selected should consider the substance of the change between the insurance enterprise and the contract holder.
- TPA 6300.27, *Changes in Investment Management Fees and Other Administrative Charges in Applying SOP 05-1*. This TPA concludes that in evaluating changes in investment management fees and other administrative charges, the insurance enterprise should first determine whether such changes are "modifications" to the contract as defined in SOP 05-1, and then apply the applicable guidance as appropriate.
- TPA 6300.28, *Definition of Reunderwriting for Purposes of Applying SOP 05-1*. This TPA concludes that the performance of examination procedures with respect to specific risks or components of a contract would not represent underwriting or reunderwriting as long as the procedures are limited in nature and do not involve judgment or discretion with respect to acceptance or price.
- TPA 6300.29, *Contract Reinstatements in Applying SOP 05-1*. This TPA concludes that if an insurance enterprise determines it has no further obligation to pay claims due to the lapse of a contract, the contract would be considered extinguished. Any subsequent reinstatement of the contract would be accounted for as a newly issued contract in the period in which the reinstatement occurs.
- TPA 6300.30, *Commissions Paid on an Increase in Insurance Coverage or Incremental Deposits in Applying SOP 05-1*. Per this TPA additional commissions incurred on either an increase in insurance coverage or incremental deposit, not previously provided for in the contract, related to a contract modification determined to result in a substantially unchanged replacement contract, should be accounted for as acquisition costs.
- TPA 6300.31, *Participating Dividends and the Interaction of Guidance in SOP 05-1 and SOP 95-1*. This TPA concludes that paid-up additions funded by dividends on participating policies that do not meet the conditions in SOP 05-1 should be accounted for in accordance with SOP 95-1, *Accounting for Certain Insurance Activities of Mutual Life Insurance Enterprises*.
- TPA 6300.32, *Premium Changes to FASB Statement No. 60 Long-Duration Contracts in Applying SOP 05-1*. This TPA concludes that the right to adjust premium rates for group long-duration insurance contracts generally would not meet the definition of a modification under SOP 05-1 as long as certain conditions are met.
- TPA 6300.33, *Evaluation of Changes Under Paragraph .15a of SOP 05-1*. This TPA concludes that a change in the period of coverage should be evaluated based on a comparison of the remaining period of coverage of the replaced contract to the remaining period of coverage of the replacement contract when assessing the significance of that change.

- TPA 6300.34, *Nature of Investment Return Rights in Paragraph .15b of SOP 05-1*. This TPA describes what constitutes the “nature of the investment return rights.”
- TPA 6300.35, *Transition Provisions for FAS 60 Long-Duration Contracts Under SOP 05-1*. This TPA concludes that the adoption of SOP 05-1 may result in a shorter life for a FASB Statement No. 60 long-duration insurance contract by changing the treatment of certain internal replacements that would have previously been anticipated and treated as continuations of the replaced contract.

For further information about the above TPAs, please go to  
[http://www.aicpa.org/download/acctstd/SOP\\_05-1\\_TPAs.pdf](http://www.aicpa.org/download/acctstd/SOP_05-1_TPAs.pdf).

### **Proposed Definition of “Settlement” in FIN 48**

The Financial Accounting Standards Board (FASB) has received inquiries asking for clarification on how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits under FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes*. Specifically, is it appropriate for an enterprise to recognize a previously unrecognized tax benefit when the only factor that has changed since determining that a benefit should not be recognized is the completion of an examination or audit by a taxing authority? To answer this and other questions, the FASB has issued proposed FASB Staff Position (FSP) No. FIN 48-a, *Definition of “Settlement” in FASB Interpretation No. 48*.

If finalized, FSP FIN 48-a would amend FIN 48 to clarify that a tax position could be effectively settled upon examination by a taxing authority, although assessing whether a tax position is effectively settled is a matter of judgment because examinations occur in a variety of ways. In determining whether a tax position is effectively settled, an enterprise should make the assessment on a position-by-position basis. When all of the following conditions have been satisfied, a tax position should be considered effectively settled through examination:

- The taxing authority has completed its examination procedures including all appeals and administrative reviews that the taxing authority is required or expected to perform for the tax position.
- The enterprise does not intend to appeal or litigate any aspect of the tax position for the completed examination.
- Based on the taxing authority’s widely understood policy, the enterprise considers it highly unlikely that the taxing authority would subsequently examine or reexamine any aspect of the tax position included in the completed examination, presuming the taxing authority has full knowledge of all relevant information.

In the tax years under examination, a tax position does not need to be specifically reviewed or examined by the taxing authority to be considered effectively settled through examination. If the taxing authority has specifically examined a tax position during the examination process, an enterprise should consider this information in assessing the likelihood that the taxing authority subsequently would re-examine that tax position for the completed examination. If an enterprise that had previously considered a tax position effectively settled becomes aware that the taxing authority may examine or re-examine the tax position, the tax position is no longer considered effectively settled and the enterprise should re-evaluate the tax position in accordance with FIN 48.

If finalized, the guidance in the proposed FSP would be effective upon the initial adoption of FIN 48. (FIN 48 is effective for years beginning after December 15, 2006.) The proposed FSP is available for comment until March 28, 2007 at [http://www.fasb.org/fasb\\_staff\\_positions/prop\\_fsp\\_fin48-a.pdf](http://www.fasb.org/fasb_staff_positions/prop_fsp_fin48-a.pdf).

## SEC

### FAQs for SAB 108

The Center for Audit Quality has issued answers to the following frequently asked questions (FAQs) regarding the implementation of SEC Staff Accounting Bulletin (SAB) 108:

1. May errors determined to be immaterial under the dual method be included in the cumulative effect adjustment upon adoption of SAB 108?
2. Are the errors that may be included in the SAB 108 cumulative effect adjustment limited to waived audit differences in prior years?
3. How should an error originating in a period prior to adoption of SAB 108 be evaluated if the error is identified subsequent to the adoption of SAB 108?
4. If a previously undetected error originating in a year subsequent to adoption of SAB 108 cannot be corrected in the year it is discovered without materially misstating that year's financial statements, and the correction to each previous period would result in immaterial adjustments to those financial statements, can the corrections be made the next time those financial statements are filed?
5. If financial statements of previous periods are determined to be immaterially misstated, what disclosures are required in the current year financial statements if they include adjustments to the prior periods to correct the immaterial errors?

The answers to these questions are based on discussions with the SEC staff and can be found in full at [http://www.aicpa.org/caq/download/AICPA\\_SAB\\_108\\_FAQ.pdf](http://www.aicpa.org/caq/download/AICPA_SAB_108_FAQ.pdf). SAB 108 can be accessed at <http://www.sec.gov/interps/account/sab108.htm>.

### Interpretive Guidance Regarding Executive Compensation

The SEC's Division of Corporation Finance has issued interpretive guidance with respect to Item 402 of Regulation S-K, *Executive Compensation*. Among other topics, the Interpretation discusses the compliance dates of the disclosure requirements and related rules adopted in the August 2006 *Executive Compensation and Related Person Disclosure* rulemaking and the related December 2006 amendments. The SEC Interpretation is available at <http://www.sec.gov/divisions/corpfin/guidance/execcomp402interp.pdf>.

## International

### Draft Standard for Small and Medium-sized Entities

The International Accounting Standards Board has released an Exposure Draft of its *International Financial Reporting Standard for Small and Medium-sized Entities* (IFRS for SMEs) to provide a simplified, self-contained set of accounting principles that are appropriate for smaller, non-listed companies and are based on full IFRS. The proposed Standard removes choices for accounting treatments, eliminates topics that are not generally relevant to SMEs, and simplifies methods for recognition and measurement.

IFRS for SMEs reduces the volume of accounting guidance applicable to SMEs by more than 85 percent as compared to the full set of IFRS. IFRS for SMEs omits the following topics, among others: price-level reporting; interim reporting; earnings per share and segment reporting; lessor accounting for finance leases; and, accounting for the recoverable amount of goodwill. Simpler accounting policy choices in IFRS for SMEs include: cost depreciation for investment property; treating all borrowing costs as expense; and, use of the indirect method for reporting operating cash flows in the cash flow statement. Simplified recognition and measurement provisions in IFRS for SMEs include: recognizing all research and development as expense; simplified hedge accounting and derecognition of financial instruments; the cost method of accounting for investments in associates and joint ventures; simplified lessee accounting for finance leases; and, use of the intrinsic value method of measuring share-based payments.

IFRS for SMEs would not be available to entities that have public accountability. Public accountability exists if the entity has issued debt or equity securities in a public market, or if the entity holds assets in a fiduciary capacity for a broad group of outsiders (e.g., a bank, insurance company, or pension or mutual fund).

The Exposure Draft is available for comment until October 1, 2007.

We expect this project will be closely followed in the United States as this continues to be a topic that attracts much attention. For example, the Financial Accounting Standards Board (FASB) and the American Institute of Certified Public Accountants (AICPA) are jointly sponsoring a new Private Company Financial Reporting Committee. This Committee is part of a broad initiative by the FASB and the AICPA to further improve the FASB's current standard-setting process to better meet the financial reporting needs of private companies and the users of their financial statements.

### **Proposal to Amend Certain Related-Party Disclosure Requirements**

The International Accounting Standards Board has published an Exposure Draft of proposed amendments to International Accounting Standard 24, *Related Party Disclosures*. The proposal would reduce the disclosure requirements for some entities that are related only because they are each state-controlled or significantly influenced by the state. The proposed exemption would be limited to those circumstances in which it is clear that the related entities are not influencing each other. Proposed indicators of circumstances in which the relationship would not be exempt include:

- The presence of common members of the board
- The existence of direction or compulsion by a state
- Related parties transacting business at non-market rates
- Related parties sharing of resources
- Related parties undertaking economically significant transactions.

The Exposure Draft also proposes certain clarifying amendments to the definition of a related party, including the following:

- The inclusion, in the definition of a related party, of the relationship between a subsidiary and an associate of the same entity, in the individual or separate financial statements of both the subsidiary and the associate.

- The removal, from the definition of a related party, of situations in which two entities are related to each other because a person has significant influence over one entity and a close member of the family of that person has significant influence over the other entity.
- The inclusion, in the definition of a related party, of two entities where one is an investee of a member of key management personnel and the other is the entity managed by the person that is a member of key management personnel.

The Exposure Draft will be available for comment from March 5 until May 25, 2007 at [www.iasb.org](http://www.iasb.org).

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