

# Insights

A biweekly publication from the National Office of Audit and Accounting

October 16, 2007

By clicking on a heading in the Bookmark section on the left, you will go directly to that subject.

## Bill Travis Appointed to Treasury Advisory Committee

Bill Travis, McGladrey & Pullen, LLP board member, has been appointed by U.S. Treasury Secretary Henry M. Paulson, Jr. to the Treasury Advisory Committee on the Auditing Profession. This committee will make recommendations as to what can be done to sustain a vibrant auditing profession, which Secretary Paulson believes is essential for a well-functioning financial reporting system in the U.S. economy. In addition to other topics, the committee will examine auditing industry concentration, financial soundness, audit quality, and employee recruitment and retention.

The Treasury Department worked with Committee Chairmen Arthur Levitt, Jr., former SEC Chairman, and Donald T. Nicolaisen, former SEC Chief Accountant, to choose members through a public nomination process. The 21 committee members represent a broad range of perspectives, including investors, auditors, large and small public companies, insurance companies, lawyers and regulators. Members include Levitt, Nicolaisen, Lynn Turner, Paul Volker, Allen Beller, and Barry Melancon, among others.

Bill Travis became McGladrey & Pullen's managing partner in 1999, serving as an architect for the firm's alternative practice structure, which has been identified as an industry model. He joined McGladrey & Pullen in 1975 as a staff accountant in the firm's Minneapolis office. He currently serves on the Governing Council of the American Institute of Certified Public Accountants (AICPA) and the Board of Trustees for the AICPA Foundation. Travis received degrees in economics, political science and philosophy from Cornell College and a master's degree in accounting from the University of Iowa.

## Accounting

### September PCFRC Meeting

The Private Company Financial Reporting Committee (PCFRC) met in Dallas, Texas on September 20-21, 2007. There were two primary activities that took place during the meeting. One of those activities was an update/status report on several Financial Accounting Standards Board (FASB) projects, including the reporting entity project, financial statement presentation, the lease accounting project, and reconsideration of FASB Statement No. 5, *Accounting for Contingencies*.

The other primary activity consisted of certain action items. The PCFRC voted unanimously to send a letter to the FASB recommending a delay of the effective date of FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes*, until clarification and guidance is issued regarding its implementation for pass-through entities (e.g., S corporations) and further consideration is given to the usefulness of FIN 48's disclosures for private companies. The PCFRC also agreed to send a letter to the FASB chairman regarding the Concept Release issued by the SEC that proposes to allow U.S. issuers to prepare financial statements in accordance with International Financial Reporting Standards. That letter will generally express support for the FASB/International Accounting Standards Board (IASB) convergence as it is

currently progressing and will remind the FASB to remain aware of the implications the convergence with IASB standards could have on private company financial reporting. Finally, the PCFRC agreed to revise a questionnaire expected to be sent to Resource Group members of the PCFRC on various aspects of FIN 46R, *Consolidation of Variable Interest Entities*. A possible outcome of this outreach project will be to send a letter to the FASB recommending that private companies be exempted from the scope of FIN 46R for certain transactions.

The next meeting of the PCFRC will be in Norwalk, Connecticut on December 6-7, 2007. A portion of that meeting will include a joint meeting with the FASB.

### **Proposed Changes to Consolidation and Equity Method Guidance for Not-for-Profits**

The Financial Accounting Standards Board (FASB) has issued a proposed FASB Staff Position (FSP), which, if finalized, would make several changes to the current guidance on consolidation and the equity method of accounting in AICPA Statement of Position (SOP) 94-3, *Reporting of Related Entities by Not-for-Profit Organizations*, and the AICPA Audit and Accounting Guide, *Health Care Organizations* (the Guide). The purpose of the proposed changes is to make the guidance more consistent between the two pronouncements and with other authoritative standards, where appropriate. FSP No. SOP 94-3-a and AAG HCO-a, *Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations*, proposes to:

- Eliminate the existing exception to consolidation for related but separate not-for-profit organizations if control is likely to be temporary, and make two related changes:
  - Amend SOP 94-3 and the Guide such that an organization would be deemed to have a *majority voting interest in the board of another entity* whenever it has the direct or indirect ability to appoint individuals that together constitute a majority of the votes of the fully constituted board.
  - Conform the categorization of sole corporate membership in SOP 94-3 to that in the Guide, i.e., sole corporate membership of one not-for-profit organization in another generally would be considered a controlling financial interest unless the sole corporate member's economic interest in the controlled entity is limited by state law or contractual agreement.
- With rare exception, confirm the continued applicability to not-for-profit lessees of the guidance on consolidation of special-purpose-entity lessors in the following Emerging Issues Task Force (EITF) Issues:
  - Issue No. 90-15, "Impact of Nonsubstantive Lessors, Residual Value Guarantees, and Other Provisions in Leasing Transactions"
  - Issue No. 96-21, "Implementation Issues in Accounting for Leasing Transactions involving Special-Purpose Entities"
  - Issue No. 97-1, "Implementation Issues in Accounting for Leasing Transactions, including Those Involving Special-Purpose Entities"
- Require not-for-profit organizations to apply the guidance on the equity method of accounting in the following pronouncements to their investments in for-profit partnerships, limited liability companies, and similar entities unless those investments are reported at fair value:
  - SOP 78-9, *Accounting for Investments in Real Estate Ventures*

- EITF Issue No. 03-16, "Accounting for Investments in Limited Liability Companies"
- FSP SOP 78-9-1, *Interaction of AICPA Statement of Position 78-9 and EITF Issue No. 04-5*.

If finalized, the guidance in this FSP would be applied to fiscal years beginning after June 15, 2008, and to interim periods therein. The proposed FSP is available for comment until November 30, 2007, at [http://www.fasb.org/fasb\\_staff\\_positions/prop\\_fsp\\_sop94-3-a&aag\\_hco-a.pdf](http://www.fasb.org/fasb_staff_positions/prop_fsp_sop94-3-a&aag_hco-a.pdf).

## SEC

### White Papers on Illiquidity in the Markets

In recent weeks the liquidity crisis that began in the subprime mortgage-related markets has spread to other corners of the credit markets and has a potentially pervasive impact on public companies generally with respect to investments held. As a result, the Center for Audit Quality Professional Practice Executive Committee has issued three white papers to address certain accounting issues arising from or related to the current illiquid market conditions:

- *Measurements of Fair Value in Illiquid (or Less Liquid) Markets* – This paper discusses issues associated with the measurement of fair value under existing generally accepted accounting principles (GAAP) in the context of illiquid (or less liquid) market conditions that currently exist in many segments of the credit markets. The paper is available in full at [http://www.aicpa.org/caq/download/WP\\_Measurements\\_of\\_FV\\_in\\_Illiquid\\_Markets.pdf](http://www.aicpa.org/caq/download/WP_Measurements_of_FV_in_Illiquid_Markets.pdf).
- *Consolidation of Commercial Paper Conduits* – This paper discusses the application of FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, by sponsors of commercial paper conduits, particularly as impacted by market conditions that currently exist in many segments of the credit markets, including illiquid (or less liquid) conditions in the commercial paper markets. The paper is available in full at [http://www.aicpa.org/caq/download/WP\\_Consolidation\\_of\\_Commercial\\_Paper\\_Conduits.pdf](http://www.aicpa.org/caq/download/WP_Consolidation_of_Commercial_Paper_Conduits.pdf).
- *Accounting for Underwriting and Loan Commitments* – This paper discusses existing GAAP associated with commitments to lend money or underwrite securities in the context of illiquid (or less liquid) market conditions that currently exist in many segments of the credit markets. The paper is available in full at [http://www.aicpa.org/caq/download/WP\\_Accounting\\_for\\_Underwriting\\_and\\_Loan\\_Commitments.pdf](http://www.aicpa.org/caq/download/WP_Accounting_for_Underwriting_and_Loan_Commitments.pdf).

The issues addressed in the white papers should be considered in light of an entity's particular facts and circumstances.

## International

### Effective Date Announced for Clarified Auditing Standards

In striving to improve the clarity of its standards, the International Auditing and Assurance Standards Board (IAASB) is continuing to redraft some of its existing standards. Recently the IAASB announced that its complete set of clarified International Standards on Auditing will be effective for audits of financial statements for periods beginning on or after December 15, 2009. Key elements of the new drafting conventions include: basing each standard on the objective of the auditor with respect to the subject matter of the standard; separating the requirements that the auditor is required to follow from guidance on their application; eliminating the present tense to describe actions by the auditor, which raised ambiguity about

whether such actions were required; and other structural and drafting improvements to enhance the overall readability and understandability of the standards. Standards redrafted in this way are described as "redrafted." If further revision has been undertaken, a standard is described as "revised and redrafted."

### **New Requirements for Audits of Group Financial Statements**

The International Auditing and Assurance Standards Board has released International Standard on Auditing (ISA) 600 (Revised and Redrafted), *Special Considerations – The Audit of Group Financial Statement (Including the Work of Component Auditors)*. This Standard provides guidance to the group engagement partner in taking responsibility for the direction, supervision and performance of the group audit and the issuance of an auditor's report that is appropriate in the circumstances. ISA 600 specifies the types of work that the group engagement team, or component auditors on its behalf, should perform on the financial information of significant components. It also requires the group engagement team to be appropriately involved in the work that component auditors perform. While the equivalent U.S. auditing standard (AU 543) states that the principal auditor may decide to make reference to the audit of an other auditor when he expresses his opinion on the financial statements, ISA 600 specifies that "the auditor's report on the group financial statements shall not refer to a component auditor, unless required by law or regulation to include such reference. If such reference is required by law or regulation, the auditor's report shall indicate that the reference does not diminish the group engagement partner's or the group engagement partner's firm's responsibility for the group audit opinion."

The ISA is effective for audits of financial periods commencing on or after December 15, 2009. ISA 600 is available in full at

<http://www.ifac.org/store/Details.tpl?SID=11914363812358813&Cart=119160919248086>.

---

*Insights* is a biweekly publication of McGladrey & Pullen, LLP and should not be construed as accounting, auditing, consulting, or legal advice on any specific facts or circumstances. The contents are intended for general information purposes only, and you are urged to consult your McGladrey & Pullen, LLP service provider concerning your situation and any specific questions you may have. You may call 1.888.214.1416 for a contact person in your area.

For further information about McGladrey & Pullen or to retrieve archived issues of *Insights*, visit our Web site: <http://www.mcgladrey.com/>. If you do not wish to continue receiving *Insights*, or if you wish to place another person on the distribution list, please contact [mpinsights@rsmi.com](mailto:mpinsights@rsmi.com).