

Insights

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Accounting

FASB Issues Statement No. 156 and Updated Implementation Guidance

The Financial Accounting Standards Board has issued Statement of Financial Accounting Standards No. 156, *Accounting for Servicing of Financial Assets*, which provides an approach to simplify efforts to obtain hedge-like (offset) accounting. This new Statement amends FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, with respect to the accounting for separately recognized servicing assets and servicing liabilities. The Statement:

- Requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in any of the following situations:
 - A transfer of the servicer's financial assets that meets the requirements for sale accounting;
 - A transfer of the servicer's financial assets to a qualifying special-purpose entity in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*;
 - An acquisition or assumption of an obligation to service a financial asset that does not relate to financial assets of the servicer or its consolidated affiliates;
- Requires that a separately recognized servicing asset or servicing liability be initially measured at fair value, if practicable;
- Permits an entity to choose either the amortization method or the fair value method for subsequent measurement for each class of separately recognized servicing assets or servicing liabilities (management determines a class based on the availability of market inputs and/or the method used for managing risks related to those assets and liabilities);
- Permits at initial adoption a one-time reclassification of available-for-sale securities to trading securities by an entity with recognized servicing rights, provided the securities reclassified offset the entity's exposure to changes in the fair value of the servicing assets or liabilities (this results in achieving hedge-like accounting and does not call into question the treatment of the other available-for-sale securities); and

- Requires separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the balance sheet and additional disclosures for all separately recognized servicing assets and servicing liabilities.

Statement No. 156 is effective for all separately recognized servicing assets and liabilities as of the beginning of an entity's fiscal year that begins after September 15, 2006, with earlier adoption permitted in certain circumstances. The Statement also describes the manner in which it should be initially applied. Appendix C of Statement No. 156 shows Statement No. 140 marked to show changes to that Statement by combining the effects of FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*, and Statement No. 156. Statement No. 156 is available in full at <http://www.fasb.org/pdf/fas156.pdf>.

Subsequent to the issuance of Statement No. 156, the FASB issued updated implementation guidance, including the Q & As from the Special Report on Statement No. 140, Statement No. 133, and EITF Issues and Topics. The updated implementation guidance is available at <http://www.fasb.org/pdf/RevisionsToRelatedLiterature.pdf>.

Preparers of financial statements are reminded of the requirement to disclose new authoritative pronouncements that have not yet been adopted. The level of information that is available to disclose before adoption of a new pronouncement will depend on a variety of circumstances.

FASB Revises SFAS 133 Implementation Guidance

The FASB has revised its *Guidance on Statement 133 Implementation Issues* as of March 14, 2006. Several Implementation Issues were revised to reflect the issuance of FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments – an Amendment of FASB Statements No. 133 and 140*, in February, 2006. The revised implementation guidance is available at <http://www.fasb.org/derivatives/issuindex.shtml>. On this page, the Implementation Issues that were affected by the update are indicated as "Revised 2/16/06."

Public Sector

GASB 45 – Are You Ready?

Currently, retiree health care costs are reported by state and local governments based on how much cash is paid out for such costs in a given year. However, Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which will be implemented in stages beginning next year, requires that all government entities report expected future retiree costs currently. GASB 45 generally requires that state and local governmental employers account for other postemployment benefits (OPEBs) in essentially the same manner as they currently do for pensions. Statement No. 45 also requires disclosure of information about the plans in which an employer participates, the funding policy followed, and the actuarial valuation process and assumptions.

An employer may establish its OPEB liability at zero as of the beginning of the initial year of implementation; however, the unfunded actuarial liability will now be disclosed, and it is required to be amortized over future periods. This accounting change may dramatically increase reported liabilities, and it will certainly call attention to future funding needs. For that reason, government entities are already obtaining actuarial valuations of their potential OPEB liabilities. Many also are considering strategies to change their health care benefits for retirees, including requiring higher health insurance co-payments, reducing levels of coverage, and providing reduced benefits for newly hired personnel.

As a reminder, Statement No. 45 is effective in three phases based on a government's total annual revenues. Governments with total annual revenues in the first fiscal year ending after June 15, 1999 of:

- \$100 million or more are required to implement this Statement in financial statements for periods beginning after December 15, 2006.
- \$10 million or more but less than \$100 million are required to implement this Statement in financial statements for periods beginning after December 15, 2007.
- Less than \$10 million are required to implement this Statement in financial statements for periods beginning after December 15, 2008.

All component units are required to implement this Statement no later than the same year as the primary government.

The GASB has published a *Guide to Implementation of GASB Statements 43 and 45 on Other Postemployment Benefits* to assist preparers and auditors of governmental financial statements as they implement Statement No. 45, as well as GASB Statement No. 43, *Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which addresses accounting by plans that administer OPEB.

Differences between Governmental and For-Profit Financial Reporting

From time to time, the question is raised as to why state and local governments cannot apply the same set of accounting standards that for-profit enterprises apply. A white paper released by the Governmental Accounting Standards Board explains why separate standards for governments are needed. It also illustrates some of the differences between standards for governments and those for business enterprises and explains why the process of standards setting for governments is an ongoing process.

According to the white paper, the primary purpose of governments is to enhance or maintain the well-being of citizens by providing services in accordance with public policy goals. In contrast, for-profit business enterprises focus primarily on wealth creation, interacting principally with those segments of society that fulfill their mission of generating a financial return on investment for shareholders. The white paper cites several other crucial differences that generate user demand for unique information:

- Governments serve a broader group of stakeholders, including taxpayers, citizens, elected representatives, oversight groups, bondholders, and others in the financial community.
- Most government revenues are raised through involuntary taxes rather than a willing exchange of comparable value between two parties in a typical business transaction.
- Monitoring actual compliance with budgeted public policy priorities is central to government public accountability reporting.
- Governments exist longer than for-profit businesses and are not typically subject to bankruptcy and dissolution.

The white paper concludes that individuals and organizations who are interested in the financial performance of state and local governments have substantially different information needs than those who follow the financial performance of for-profit entities. The white paper is available in full at http://www.gasb.org/white_paper_full.pdf.

International

Amendments to IAS 1 Proposed

The International Accounting Standards Board (IASB) has published an Exposure Draft of proposed amendments to International Accounting Standard (IAS) 1, *Presentation of Financial Statements*. The Exposure Draft results from the first stage of the IASB's project on performance reporting and, if confirmed, would bring IAS 1 largely into line with the equivalent U.S. standard. The second stage is being undertaken jointly with the Financial Accounting Standards Board and includes a reconsideration of the presentation and display of information in the financial statements. Under the proposed exposure draft, an entity would present all income and expenses separately from changes in its equity that arise from transactions with its owners. Entities would have a choice of presenting income and expenses in a single statement or in two statements. An entity also would be required to include in its set of financial statements a statement showing its financial position (or balance sheet) at the beginning of the previous period. The Exposure Draft is available for comment until July 17, 2006.

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