

Insights

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Accounting

Proposed Revision to Definition of a Public Entity

Certain authoritative accounting pronouncements define a public entity as:

An enterprise that has issued debt or equity securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets), that is required to file financial statements with the Securities and Exchange Commission, or that provides financial statements for the purpose of issuing any class of securities in a public market.

Recently, questions have been raised as to whether a conduit bond obligor for conduit debt securities that are traded in a domestic or foreign stock exchange or an over-the-counter market should be considered a public entity for the purposes of applying certain existing authoritative pronouncements. *Conduit debt securities* refers to certain limited-obligation revenue bonds, certificates of participation, or similar debt instruments issued by a state or local governmental entity for the express purpose of providing financing for a specific third party that is not a part of the state or local government's financial reporting entity. The third party (conduit bond obligor) is required to make all interest and principal payments as they become due, and any future financial reporting requirements are the responsibility of the conduit bond obligor. The definition of a conduit bond obligor includes all individual conduit bond obligors that participate in a pooled conduit municipal bond. The types of private entities that can be involved in a conduit municipal bond are limited by the federal tax code to certain not-for-profit entities (for example, hospitals, museums, and libraries) and to for-profit entities for whom the debt is issued in the form of an industrial revenue or development bond that is issued for a specific purpose allowable by the Internal Revenue Code. In some instances, these conduit municipal bonds are traded in a public market.

Proposed FASB Staff Position (FSP) No. FAS 126-a, *Revision to the Definition of a Public Entity to Include an Obligor for Conduit Debt Securities*, concludes that the definition of a public entity in the following standards should be amended to include an entity that is a conduit bond obligor for conduit debt securities that are traded in a public market:

- APB Opinion No. 28, *Interim Financial Reporting*;
- FASB Statement No. 69, *Disclosures about Oil and Gas Producing Activities*;
- FASB Statement No. 109, *Accounting for Income Taxes*;
- FASB Statement No. 126, *Exemption from Certain Required Disclosures about Financial Instruments for Certain Nonpublic Entities*;
- FASB Statement No. 131, *Disclosures about Segments of an Enterprise and Related Information*,
and

- FASB Statement No. 141, *Business Combinations*.

The effects of applying proposed FSP No. FAS 126-a are expected to be recognized as a change in accounting principle through retrospective application to all prior periods unless it is impracticable to do so. The proposed FSP is available for comment until July 31, 2006, at http://www.fasb.org/fasb_staff_positions/prop_fsp_fas126-a.pdf.

Revised Guidance for SFAS 133 Implementation Issues

The Financial Accounting Standards Board (FASB) has posted revised guidance for certain Implementation Issues related to FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. The revised Issues were affected by the issuance of FASB Statement No. 156, *Accounting for Servicing of Financial Assets*, as well as other revisions related primarily to FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*. The newly revised guidance for Issues posted on June 16, 2006, marked for changes from the most recent prior guidance, is available at <http://www.fasb.org/derivatives/06-16-06.pdf>. The complete listing of all Implementation Issues is available at <http://www.fasb.org/derivatives/issuindex.shtml>.

SEC

Mark Olson Named PCAOB Chairman

Federal Reserve Board Governor Mark W. Olson has been appointed Chairman of the Public Company Accounting Oversight Board (PCAOB) until 2010. Mr. Olson will succeed Acting Chairman Bill Gradison, who will remain a member of the Board.

Mr. Olson began his banking career in 1966 with First Bank System and was named an officer in 1969. From 1976 to 1988, he was President and CEO of Security State Bank and also served as President of the American Bankers Association. From 1988 to 1999, Mr. Olson was a partner with Ernst & Young LLP and its predecessor, Arthur Young & Company. At Ernst & Young, he was National Director of the firm's Regulatory Consulting Practice for the financial services industry.

During 2000 and 2001, Mr. Olson served as Staff Director of the U.S. Senate Securities Subcommittee of the Banking, Housing, and Urban Affairs Committee. Mr. Olson joined the Federal Reserve in 2001, where he has served as Administrative Governor being responsible for management of the Federal Reserve Board since 2002. Mr. Olson also serves on the Federal Reserve Board Committee on Supervisory and Regulatory Affairs and is the Chairman of the Committee on Consumer and Community Affairs.

International

Revised Guidance Proposed for Certain Financial Instruments

International Accounting Standard (IAS) 32, *Financial Instruments: Presentation*, requires a financial instrument to be classified as a liability if the holder of that instrument can require the issuer to redeem it for cash. Many instruments, including some ordinary shares and partnership interests, include provisions that allow the holder to "put" the instrument (to require the issuer to redeem it) for cash. Such instruments, which would otherwise be considered as equity, must be classified as liabilities under the existing provisions of IAS 32.

The International Accounting Standards Board (IASB) believes that there are many legitimate reasons for put features that should not necessarily cause the related instruments to be classified as liabilities.

Therefore the IASB has published proposals which would allow some instruments to be classified as equity rather than as liabilities. Under the proposed amendments, the following types of financial instruments would be classified as equity, provided that specified criteria are met:

- Ordinary shares that are puttable to (redeemable from) the issuer at fair value;
- Ordinary shares of limited-life entities; and
- Partners' interests in a partnership that must liquidate upon exit of a partner (e.g., on retirement or death).

The amendments also propose disclosures about the instruments affected by the proposals, including the fair value of puttable instruments classified as equity. The proposals are set out in an Exposure Draft of proposed amendments to IAS 32 and IAS 1, *Presentation of Financial Statements*. The Exposure Draft will be available for comment from July 3, 2006, to October 23, 2006, at <http://www.iasb.org/>.

The IASB plans to comprehensively review the treatment of all financial instruments in its joint long-term project on liabilities and equity with the Financial Accounting Standards Board. The project's objective is to develop a comprehensive standard of accounting and reporting for financial instruments with characteristics of equity, liabilities, or both, and assets.

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