

Insights

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Accounting

Determining the Fair Value of a Financial Asset when the Market for that Asset Is Not Active

On October 10, 2008, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) No. FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*. This FSP amends FASB Statement No. 157, *Fair Value Measurements*, by clarifying its application by providing an example to illustrate key considerations in determining the fair value of a financial asset when the market for that asset is not active. Application issues include: (a) how a reporting entity's own assumptions should be considered when measuring fair value when relevant observable inputs do not exist; (b) how available observable inputs in a market that is not active should be considered when measuring fair value; and (c) how the use of market quotes should be considered when assessing the relevance of observable and unobservable inputs available to measure fair value.

The key existing principles of Statement No. 157 that are illustrated in the example include:

- A fair value measurement represents the price at which a transaction would occur between market participants at the measurement date. In situations in which there is little, if any, market activity for an asset at the measurement date, the fair value measurement objective remains the same - that is, the price that would be received by the holder of the financial asset in an orderly transaction that is not a forced liquidation or distressed sale at the measurement date.
- In determining fair value for a financial asset, the use of a reporting entity's own assumptions about future cash flows and appropriately risk-adjusted discount rates is acceptable when relevant observable inputs are not available. In some cases an entity may determine that observable market inputs (Level 2) require significant adjustment based on unobservable data and thus would be considered a Level 3 fair value measurement. Regardless of the valuation technique used, an entity must include appropriate risk adjustments that market participants would make for nonperformance and liquidity risks.
- Broker (or pricing service) quotes may be an appropriate input when measuring fair value, but they are not necessarily determinative if an active market does not exist for the financial asset. In an active market, a broker quote should reflect market information from actual transactions. However, when markets are not active, brokers may rely more on models with inputs based on the information available only to the broker. In weighing a broker quote as an input to a fair value measurement, an entity should place less reliance on quotes that do not reflect the result of market transactions.

The FSP includes a reminder that for recurring fair value measurements using significant unobservable inputs (Level 3), Statement No. 157 requires an entity to reconcile the beginning and ending balances, including separately presenting changes that occurred during the period that are attributable to transfers in

and/or out of Level 3. For both recurring and nonrecurring fair value measurements using significant unobservable inputs (Level 3), Statement No. 157 requires an entity to describe the inputs and the information used to develop those inputs.

The FSP was effective upon issuance on October 10, 2008, including prior periods for which financial statements have not been issued. Revisions resulting from a change in the valuation technique or its application should be accounted for as a change in accounting estimate.

The FSP is available in full at http://www.fasb.org/pdf/fsp_fas157-3.pdf.

Tax Accounting Issues Related to Unrealized Losses on Available-for-Sale Equity Securities

When a reporting entity has unrealized losses on equity securities classified as available for sale, the entry is reported in the FASB Statement 115 component of other comprehensive income for financial reporting purposes. However, for income tax purposes, a loss will not be recognized until such time as the securities are sold or deemed to be worthless. This difference in the treatment for financial reporting vs. income tax purposes results in a deferred tax asset.

Investments in equity securities classified as available for sale are generally considered to be “capital assets” under the tax laws. Therefore, any losses recognized for tax purposes will be considered capital losses. A corporation may use capital losses only to offset capital gains, not ordinary income. Thus, a reporting entity will only realize a tax benefit from the loss on these securities to the extent that it also has capital gains. See, however, an article in the “Financial Institutions” section below regarding tax accounting issues related to investments in the Federal National Mortgage Association and the Federal Home Mortgage Corporation.

Reporting entities may find it difficult to generate sufficient capital gains against which the capital losses may be deducted. The deferred tax asset may or may not ever be realized. Therefore, reporting entities need to consider whether a valuation allowance for the deferred tax asset is necessary.

Per FASB Statement No. 109, *Accounting for Income Taxes*, future realization of the tax benefit of an existing deductible temporary difference or carryforward ultimately depends on the existence of sufficient taxable income of the appropriate character (for example, ordinary income or capital gain) within the carryback/carryforward period available under the tax law. Per Statement No. 109, an entity should reduce a deferred tax asset (by use of a valuation allowance) for a capital loss unless there are sufficient capital gains to offset the capital loss. The reporting entity needs to provide evidence that there are one or more sources of taxable income sufficient to support a conclusion that a valuation allowance is not necessary.

If a reporting entity has recognized capital gains in prior years, and anticipates selling its equity securities classified as available for sale by a date such that the loss could be carried back to a year when capital gains were recognized, then documentation of management’s intention and ability to carry out this plan may be sufficient evidence to support a conclusion that a valuation allowance is not necessary. In other cases, it may be necessary for management to document their tax-planning strategy that they intend to utilize to realize the tax benefit.

If a reporting entity recognizes a deferred tax asset relating only to a net unrealized loss on available-for-sale securities and at the same time concludes that it is more likely than not that some or all of that deferred tax asset will not be realized, the entry for the valuation allowance is reported in the Statement 115 component of other comprehensive income because the valuation allowance is directly related to the unrealized holding loss on the available-for-sale securities. The entry for the valuation allowance also would be reported in the Statement 115 component of other comprehensive income if the enterprise reaches its

conclusion on the need for a valuation allowance in a later interim period of the same fiscal year in which the deferred tax asset is initially recognized.

If a reporting entity does not need to recognize a valuation allowance at the same time that it establishes a deferred tax asset relating to a net unrealized loss on available-for-sale securities but in a subsequent fiscal year concludes that it is more likely than not that some or all of that deferred tax asset will not be realized, a valuation allowance is required to be recognized. The offsetting entry should be included as an item in determining income from continuing operations. It should not be included in other comprehensive income.

If a reporting entity recognizes a deferred tax asset relating to a net unrealized loss on available-for-sale securities and at the same time concludes that a valuation allowance is warranted and in a subsequent fiscal year makes a change in judgment about the level of future years' taxable income such that all or a portion of that valuation allowance is no longer warranted, any reversals in the valuation allowance due to such a change in judgment in subsequent fiscal years should be included as an item in determining income from continuing operations, even though initial recognition of the valuation allowance affected the Statement 115 component of other comprehensive income. If, rather than a change in judgment about future years' taxable income, the reporting entity generates taxable income in the current year that can utilize the benefit of the deferred tax asset, the reduction of the valuation allowance is allocated to that taxable income.

Implications of Liquidity Restrictions

The AICPA staff recently issued Technical Practice Aid (TPA) - *TIS Section 1100, Statement of Financial Position - .15 Liquidity Restrictions*. This TPA addresses the following potential accounting and auditing implications when a fund or its trustee imposes restrictions on a nongovernmental entity's ability to withdraw its balance in a money-market fund or other short-term investment vehicle:

- Balance sheet classification (e.g., whether the asset is a cash equivalent and whether all or any portion of the asset may be classified as a current asset)
- Financial statement disclosures
- Violations of debt covenants
- Events occurring subsequent to the balance sheet date, but prior to the issuance of the financial statements (e.g., significant changes in fair value or changes in liquidity)
- The entity's ability to continue as a going concern
- Auditor communication with those charged with governance
- The emphasis of a matter in the auditor's report

The TPA is available in full at http://www.aicpa.org/download/acctstd/TIS1100_15.pdf.

FASB Votes to Propose Deferral of FIN 48 for Private Entities

At its October 1, 2008 meeting, the Financial Accounting Standards Board (FASB) voted to propose a one-year deferral of the effective date of FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes*, for pass-through entities such as Subchapter S corporations, partnerships, and LLC entities. After that decision was made, questions were raised as to whether such a proposal would apply to all entities within a chain of entities if a pass-through entity existed anywhere within the chain. Additionally, questions

were raised regarding whether cooperatives, real estate investment trusts, and hedge funds were considered to be pass-through entities.

To avoid the complexities of addressing how to define the term “pass-through,” the FASB has reconsidered the scope of its proposed one-year deferral of the effective date of FIN 48 for certain private enterprises. At its October 15, 2008 meeting, the FASB voted to expand the scope of the proposed deferral so that it now includes all private entities, including privately owned C corporations. Under the expanded proposal, FIN 48 would be effective for private entities for annual periods beginning after December 15, 2008 if they have not yet issued a full set of U.S. GAAP annual financial statements incorporating the recognition, measurement, and disclosure requirements of FIN 48. Early adoption is still permitted.

The definition of “nonpublic enterprise” for this deferral is expected to be the same as the definition in FASB Statement No. 109, *Accounting for Income Taxes*, which are entities other than (a) those with debt or equity securities that trade in a public market, (b) those who are filing to register securities, and (c) conduit bond obligors for conduit debt securities that are traded in a public market. Our firm therefore believes that nonpublic consolidated entities of public companies that apply U.S. GAAP will not be eligible for the deferral for their stand-alone financial statements. U.S. subsidiaries of a foreign public company that applies U.S. GAAP and conduit bond obligors for conduit debt securities that are traded in a public market also would not be eligible for the deferral. However, a nonpublic company that is wholly- or majority-owned by a publicly traded company and that is included in the public company’s consolidated financial statements at fair value (for example, a private company owned by a publicly traded private equity group) would be eligible for the deferral for its stand-alone financial statements.

The proposed deferral of FIN 48 will be exposed for public comment through a proposed FASB Staff Position (FSP). Upon issuance, the FSP is expected to be subject to a 30-day public comment period after which the FASB will make its final decision on whether to delay the effective date for private entities. Since the delay is not “official” until the final vote by the FASB, any financial statements issued before then for periods that began after December 15, 2007 must include the adoption of FIN 48. When the FSP is issued for public comment, *Insights* will summarize the important provisions of the FSP.

Proposed Statements on Going Concern and Subsequent Events

The Financial Accounting Standards Board (FASB) recently issued two separate but related Exposure Drafts (EDs) of proposed FASB Statements - *Going Concern* and *Subsequent Events*. If finalized, these proposed Statements would incorporate accounting guidance that originated as auditing standards into the body of authoritative literature issued by the FASB, and also narrow the differences between U.S. generally accepted accounting principles (GAAP) and International Financial Reporting Standards.

The proposed Statement on going concern would require that management of a reporting entity consider all available information about the future, which is at least, but not limited to, 12 months from the end of the reporting period, when assessing whether a going-concern assumption is appropriate. (Prior to the issuance of this proposed Statement, the time horizon for the going concern assessment was limited to one year beyond the date of the financial statements.) The proposed Statement also would require disclosures when either the financial statements are not prepared on a going-concern basis or there is substantial doubt as to an entity’s ability to continue as a going concern.

The proposed Statement on subsequent events establishes general standards of accounting for and disclosure of events that occur subsequent to the balance sheet date but before financial statements are issued or available to be issued (*i.e.*, complete in a form and format that complies with GAAP and approved

for issuance). The proposed Statement would require disclosure of the date through which management has evaluated subsequent events and the basis for that date, that is, whether that date represents the date the financial statements were issued or the date the financial statements were available to be issued. There are two types of subsequent events to be evaluated:

- Recognized subsequent events - An entity must recognize in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements.
- Nonrecognized subsequent events - An entity must not recognize subsequent events that provide evidence about conditions that did *not* exist at the date of the balance sheet but that arose after the balance sheet date. Some nonrecognized subsequent events may be of such a nature that they must be disclosed to keep the financial statements from being misleading. For such events, an entity must disclose the nature of the event and an estimate of its financial effect or a statement that such an estimate cannot be made.

If finalized, the proposed Statements would be effective for interim or annual financial statements issued after ratification of the FASB Accounting Standards Codification and would be applied prospectively. The FASB believes that neither Statement will have a significant effect on current practice.

The EDs are available for comment until December 8, 2008 at <http://www.fasb.org/draft/index.shtml>.

Discussion Paper on Financial Statement Presentation

Currently, International Financial Reporting Standards and U.S. generally accepted accounting principles (GAAP) provide only limited financial statement presentation guidance. In addition, presentation guidelines in U.S. GAAP are dispersed across standards. Further, users of financial statements have expressed dissatisfaction that information is not linked across the different statements and that dissimilar items are in some cases aggregated in one number. To address these issues, the International Accounting Standards Board and the Financial Accounting Standards Board (the Boards) have published for public comment a Discussion Paper, *Preliminary Views on Financial Statement Presentation*.

The Discussion Paper contains an analysis of the current issues in financial statement presentation and presents the Boards' initial thinking on how those issues could be addressed in a possible future format. A principle-based format is presented in the Discussion Paper to achieve two main objectives for financial statement presentation:

- Cohesiveness – to ensure that a reader of financial statements can follow the flow of information through the different statements of an entity; and
- Disaggregation - to ensure that items that respond differently to economic events are shown separately.

The Boards believe there should be three basic financial statements - namely a statement of financial position, comprehensive income, and cash flows. Each of those financial statements would have sections on the core business, financing activities, income taxes, and discontinued operations. The Boards expect to publish an Exposure Draft setting forth their tentative conclusions in 2010.

The Discussion Paper is available for comment until April 14, 2009 at http://www.fasb.org/draft/DP_Financial_Statement_Presentation.pdf.

Auditing

Guidance Revised for Communicating Internal Control Related Matters

The Auditing Standards Board has issued Statement on Auditing Standards (SAS) No. 115, *Communicating Internal Control Related Matters Identified in an Audit*. SAS No. 115 conforms the definitions of the various kinds of deficiencies in internal control and the related guidance for evaluating such deficiencies in AU Section 325, *Communicating Internal Control Related Matters Identified in an Audit*, with the definitions and guidance in Statement on Standards for Attestation Engagements (SSAE) No. 15 (AT 501), *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements*. SSAE No. 15 aligned the definitions of the various kinds of deficiencies in internal control and the related guidance for evaluating such deficiencies with the definitions and guidance in Public Company Accounting Oversight Board Auditing Standard No. 5, *An Audit of Internal Control That is Integrated with an Audit of Financial Statements*. SAS No. 115 provides the following definitions:

- A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.
 - A deficiency in design exists when (a) a control necessary to meet the control objective is missing; or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met.
 - A deficiency in operation exists when (a) a properly designed control does not operate as designed; or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.
- A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.
- A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

SAS No. 115 revises the list of deficiencies in internal control that are indicators of material weaknesses, and no longer includes a list of deficiencies that ordinarily would be considered at least significant deficiencies. The Statement contains a revised illustrative written communication of material weaknesses and significant deficiencies to management and those charged with governance. SAS No. 115 supersedes SAS No. 112 of the same title.

SAS No. 115 is effective for audits of financial statements for periods ending on or after December 15, 2009. Earlier implementation is permitted.

Financial Institutions

Tax Accounting Issues Related to Investments in FNMA and FHMC

Recently, the U.S. Treasury Department placed the Federal National Mortgage Association (FNMA) and the Federal Home Mortgage Corporation (FHMC) into conservatorship. As a result, most financial institutions that hold common or preferred stock in these government-sponsored entities (GSEs) are

recording other-than-temporary impairment (OTTI) charges for financial reporting purposes. However, as long as these stocks continue to trade on an exchange, they will not be considered worthless under tax law. While financial institutions will likely recognize an OTTI loss related to common and preferred stock they hold in the GSEs for financial reporting purposes in the third quarter of 2008, a tax loss will not be recognized until such time as the stock is sold or deemed to be worthless. This difference in the treatment for financial reporting vs. tax purposes results in a deferred tax asset related to the OTTI charge.

Investments in the common and preferred stock of the GSEs are considered to be "capital assets" under the tax laws. Therefore, any losses recognized for tax purposes will be considered capital losses. A corporation may use capital losses only to offset capital gains, not ordinary income. Thus, a financial institution will only realize a tax benefit from the loss on these stocks to the extent that the financial institution also has capital gains.

On October 3, 2008, President Bush signed into law the *Emergency Economic Stabilization Act of 2008* (EESA). Section 301 of the EESA included a provision to consider investments in the common and preferred stock of FHMC and FNMA to be "ordinary assets" rather than "capital assets". Thus, financial institutions are more likely to enjoy a tax benefit as a result of recognizing a loss on the sale of FHMC or FNMA stock. Financial institutions should be aware, however, that any need for a deferred tax valuation allowance as of September 30, 2008 must be based on the enacted law at September 30, 2008. Accordingly, it is possible that a financial institution would record a deferred tax valuation allowance at September 30 and then a reversal of the deferred tax valuation allowance in the next quarter as a result of the subsequent change in characterization of the losses to ordinary.

The federal banking and thrift regulatory agencies announced on October 17, 2008, that they will allow banks, bank holding companies, and thrifts (collectively, "banking organizations") to recognize the effect of the tax change enacted in Section 301 of the EESA in their third-quarter 2008 regulatory capital calculations. This decision by the agencies will allow banking organizations to recognize the economic benefits of the change in the tax treatment of losses on FNMA and FHMC preferred stock under Section 301 of the EESA in the third quarter of 2008 for regulatory capital purposes. The agencies plan to provide regulatory reporting instructions to banking organizations describing how the effect of the tax change enacted in Section 301 of EESA should be reflected in the measurement of regulatory capital in their regulatory reports for September 30, 2008.

SEC Chief Accountant Clarifies Impairment Accounting Rules for PPS

In a letter addressed to the chairman of the Financial Accounting Standards Board (FASB), dated October 14, 2008, SEC Chief Accountant Conrad Hewitt clarified the SEC staff's view of how companies should apply impairment accounting rules in the face of declines in value of certain perpetual preferred securities (PPS). These securities are often structured in equity form but generally possess significant "debt-like" characteristics. However, because these instruments are not required to be redeemed by the issuer, nor are they redeemable at the option of the investor, these securities are classified as equity securities under FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*.

While Statement No. 115 provides guidance on the balance sheet classification of these securities, the Standard does not specifically address the impact, if any, of the debt-like characteristics of the PPS on the assessment of other-than-temporary impairment (OTTI). Given the hybrid nature of these investments and the uncertainty regarding this issue, the SEC's Office of the Chief Accountant (OCA), after consultation with and concurrence of the staff of the FASB, has concluded that it would not object to an issuer, for impairment tests in filings subsequent to October 14, 2008, applying an impairment model (including an

anticipated recovery period) similar to a debt security. The OCA would not object to this treatment, provided there has been no evidence of a deterioration in credit of the issuer, until this matter can be addressed further by the FASB. The OCA would expect an issuer to provide adequate disclosure about their PPS holdings in situations where the cost exceeds the current fair value as required by FASB Staff Position No. FAS 115-1 and 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. Disclosure should include sufficient detail to allow investors to understand the information considered in reaching the conclusion that the impairment is not other than temporary and the factors considered in concluding that there was no evidence of credit deterioration in the PPS securities.

Mr. Hewitt considers the clarification given in his October 14, 2008 letter to be an intermediate step in addressing the practice issues that exist in the application of the OTTI model to PPS. The OCA has requested the FASB to expeditiously address issues that have arisen in the application of the OTTI model in Statement No.115.

Mr. Hewitt's letter is available in full at <http://www.sec.gov/info/accountants/staffletters/fasb101408.pdf>.

SEC

PCAOB Proposes New Auditing Standards

The Public Company Accounting Oversight Board (PCAOB) has proposed for public comment a suite of seven new auditing standards related to the auditor's assessment of and responses to risk and related conforming amendments. The proposals build upon and attempt to improve the existing framework for risk assessment by, among other things, taking account of improvements in risk assessment methodologies, enhancing the integration of the risk assessment standards with the standard for the audit of internal control over financial reporting, emphasizing the auditor's responsibilities for considering the risk of fraud as being a central part of the audit process, and reducing unnecessary differences with the risk assessment standards of other auditing standard setters. There is a degree of commonality between the proposed standards and the recently updated risk assessment standards of the International Auditing and Assurance Standards Board, though they do not mirror them word-for-word.

The proposed risk assessment standards are:

- *Audit Risk in an Audit of Financial Statements* describes the components of audit risk and the auditor's responsibilities for reducing audit risk to an appropriately low level in order to obtain reasonable assurance in an audit of financial statements.
- *Audit Planning and Supervision* describes the auditor's responsibilities for planning the audit, including assessing matters that are important to the audit, and establishing an appropriate audit strategy and audit plan. The proposed standard also describes the responsibilities of the engagement partner and other engagement team members for supervising and reviewing the work of the engagement team.
- *Identifying and Assessing Risks of Material Misstatement* describes the auditor's responsibilities for identifying and assessing risks of material misstatement.
- *The Auditor's Responses to the Risks of Material Misstatement* sets forth the auditor's responsibilities for responding to the risks of material misstatement in the general conduct of the audit and specific audit procedures.
- *Evaluating Audit Results* describes the auditor's responsibilities regarding the process of evaluating the results of the audit in order to form the opinion(s) to be presented in the auditor's report.

- *Consideration of Materiality in Planning and Performing an Audit* sets forth the auditor's responsibilities for applying the concept of materiality, as described by the federal securities laws, in planning the audit and determining the scope of the audit procedures.
- *Audit Evidence* sets forth the auditor's responsibilities regarding designing and applying audit procedures to obtain sufficient appropriate evidence to support the opinion(s) in the auditor's report.

The proposed standards are available for comment until February 18, 2009 at http://www.pcaobus.org/Rules/Docket_026/2008-10-21_Release_No_2008-006.pdf.

International

IAASB Issues Audit Practice Alert

To assist auditors in addressing the challenges of auditing fair value accounting estimates, the staff of the International Auditing and Assurance Standards Board (IAASB), has released a Staff Audit Practice Alert, *Challenges in Auditing Fair Value Accounting Estimates in the Current Market Environment*. The purpose of the Alert is to highlight areas within the International Standards on Auditing (ISAs) that are particularly relevant in auditing fair value accounting estimates in times of market uncertainty. The Alert does not amend or override the ISAs that are currently effective, but rather is intended to remind auditors of certain obligations under those standards. The Alert also directs auditors to the recently revised ISA 540 (Revised and Redrafted), *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*. While not effective until audits of financial periods commencing on or after December 15, 2009, it includes guidance that is likely to be useful to auditors in planning their 2008 engagements.

The Alert has been prepared in light of current difficulties in the credit markets, and therefore has a focus on financial instruments. It also refers to related issues concerning whether an entity has the ability to continue as a going concern. The Alert is relevant to audits of all entities that have investments in financial instruments, especially those in illiquid markets.

The Alert may be downloaded free of charge at http://web.ifac.org/download/Staff_Audit_Practice_Alert.pdf.

IASB Permits Reclassification of Financial Instruments

The International Accounting Standards Board (IASB) recently issued an amendment to International Accounting Standard (IAS) 39, *Financial Instruments: Recognition and Measurement*, and International Financial Reporting Standard (IFRS) 7, *Financial Instruments: Disclosures*, to permit the reclassification of some financial instruments. *Reclassification of Financial Assets* permits an entity to reclassify non-derivative financial assets (other than those designated at fair value through profit or loss by the entity upon initial recognition) out of the fair value through profit or loss category in particular circumstances. The amendments also permit an entity to transfer from the available-for-sale category to the loans and receivables category a financial asset that would have met the definition of loans and receivables (if the financial asset had not been designated as available for sale), if the entity has the intention and ability to hold that financial asset for the foreseeable future.

Prior to these amendments IAS 39 did not permit financial instruments to be reclassified into or out of the fair value through profit or loss category while being held or issued. The amendments to IAS 39 introduce the possibility of reclassifications for companies applying IFRS, which were already permitted under U.S. generally accepted accounting principles in rare circumstances. FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, permits a security to be reclassified out of the trading

category in extremely rare situations. FASB Statement No. 65, *Accounting for Certain Mortgage Banking Activities*, permits loans to be reclassified out of the held-for-sale category if the company has the intention and ability to hold the loan for the foreseeable future or until maturity.

A company should apply the IASB amendments from July 1, 2008. Any reclassifications of a financial asset made in periods beginning on or after November 1, 2008 should take effect only from the date when the reclassification is made. Any reclassification should not be applied retrospectively to reporting periods ended before July 1, 2008.

Proposals to Improve Disclosures about Financial Instruments

The International Accounting Standards Board (IASB) has been informed by users of financial statements and others that enhanced disclosures about fair value measurements are needed, especially in light of the present market conditions. Many suggested that the IASB consider disclosures similar to those included in FASB Statement No. 157, *Fair Value Measurements*, which are based on a three-level hierarchy for the inputs to the valuation techniques that are used to measure fair value. The IASB therefore has issued an Exposure Draft (ED), *Improving Disclosures about Financial Instruments*, which would amend the disclosure requirements in International Financial Reporting Standard 7, *Financial Instruments: Disclosures*, based on a three-level fair value hierarchy (similar to the hierarchy in FASB Statement No. 157). The amendments would apply to financial instruments and require disclosures about:

- The level of the fair value hierarchy into which fair value measurements are categorized in their entirety. This requirement would apply both for fair values included in the statement of financial position and for other fair values that are disclosed but not included in that statement.
- The fair value measurements resulting from the use of significant unobservable inputs to valuation techniques. For these measurements, the disclosures include a reconciliation from the beginning balances to the ending balances.
- The movements between different levels of the fair value hierarchy, and the reasons for those movements.

The IASB also was informed that some of the existing disclosure requirements about the nature and extent of liquidity risk were unclear and difficult to apply and did not always result in useful information for users of financial statements. Therefore the ED also includes amendments which would:

- Clarify that liquidity-risk disclosures are required only for financial liabilities that will result in the outflow of cash or another financial asset.
- Require entities to provide quantitative disclosures based on how they manage liquidity risk for derivative financial liabilities.
- Require entities to disclose the remaining expected maturities of non-derivative financial liabilities if they manage liquidity risk on the basis of expected maturities.
- Strengthen the relationship between qualitative and quantitative disclosures about liquidity risk.

If finalized, the amendments would be effective for annual periods beginning on or after July 1, 2009, with earlier application permitted. The ED is available for comment until December 15, 2008 at

http://www.iasb.org/NR/rdonlyres/1EB5581B-A460-40AF-9F66-0B9314A46C32/0/ED_AmendmentstoIFRS7_WEBSITE.pdf.

Discussion Paper on Financial Statement Presentation

Currently, International Financial Reporting Standards and U.S. generally accepted accounting principles (GAAP) provide only limited financial statement presentation guidance. In addition, presentation guidelines in U.S. GAAP are dispersed across standards. Further, users of financial statements have expressed dissatisfaction that information is not linked across the different statements and that dissimilar items are in some cases aggregated in one number. To address these issues, the International Accounting Standards Board and the Financial Accounting Standards Board have published for public comment a Discussion Paper, *Preliminary Views on Financial Statement Presentation*. For further information about this Discussion Paper, please see a related article, "Discussion Paper on Financial Statement Presentation," in the "Accounting" section above.

Get Up to Speed with IFRS

This article is the sixth in a series of articles that takes our readers on a journey through International Financial Reporting Standards (IFRS) with a special focus on the standards' quintessential feature: they are principles-based. In this article, we provide advice to help professionals manage the changeover from U.S. generally accepted accounting principles (GAAP) to IFRS.

The SEC recently voted to publish a proposed multi-year plan setting out several milestones that could lead to the use of IFRS by U.S. issuers beginning in 2014. The SEC will make a decision in 2011 on whether the adoption of IFRS is in the public interest. However, the actual publishing of a proposed roadmap signals the coming of IFRS. Fortunately, there is still time to prepare for the implementation of IFRS. It is, however, important that professionals who will be involved with IFRS start working on their personal professional development plan for learning about IFRS. Following are some suggestions to help design and manage the learning process:

- Start a personal toolkit. This toolkit should consist of information that is available on the International Accounting Standards Board Web site, such as *A Guide through International Financial Reporting Standards July 2008*. There are also newsletters from various sources that provide useful up-to-date information. Further, public-company financial statements that have been prepared in accordance with IFRS are available on the Internet.
- Commit to self-study of IFRS and a full understanding of the philosophy behind it. On the Internet, there is a significant quantity of material that can be accessed free-of-charge or via subscription.
- Attend IFRS training courses. There are a variety of courses that are currently available. Following are some points to consider as you evaluate courses:
 - Select the right level to address your needs. Overviews, IFRS vs. U.S. GAAP comparisons, or other courses that cover many topics in a few hours might be appropriate for beginners but not for those seeking in-depth training.
 - Insist that instructors have fieldwork experience in applying IFRS.
 - Ask for evaluations from previous training offerings.
- Build your own consultation network. Professionals should start thinking now about how they will be able to resolve IFRS implementation issues, possibly in consultation with others.

In conclusion, approaching a new set of standards requires a significant investment of time and effort. Particularly, one way or another, professionals will have to go back to “school”. This might sound obvious, but not underestimating this inevitable and preliminary step represents a good starting point.

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