AICPA International Practices Task Force Meeting Highlights

May 3, 2001

Location: AICPA Washington Office

NOTICE: The AICPA SEC Regulations Committees International Practices Task Force meets periodically with the staff of the SEC to discuss emerging technical accounting and reporting issues relating to SEC rules and regulations. The purpose of the following highlights is to summarize the issues discussed at the meetings. These highlights have not been considered and acted on by senior technical committees of the AICPA, or by the Financial Accounting Standards Board, and do not represent an official position of either organization.

In addition, these highlights are not authoritative positions or interpretations issued by the SEC or its staff. The highlights were not transcribed by the SEC and have not been considered or acted upon by the SEC or its staff. Accordingly, these highlights do not constitute an official statement of the views of the Commission or of the staff of the Commission.

I. ATTENDANCE

Richard Dieter, Chairman (Arthur Andersen)
Wayne Carnall (PricewaterhouseCoopers)
Ed Cannizzaro (KPMG)
Paul Dudek (SEC Observer)
D.J. Gannon (Deloitte & Touche)
Roger Jahncke (Ernst & Young)
Joseph Kelley (KPMG)
Craig Olinger (SEC Observer)
Joel Osnoss (Deloitte and Touche)
Eric Phipps (Arthur Andersen)
Carol Riehl (Grant Thornton)
Annette Schumacher Barr (AICPA)
Lisa Vanjoske (SEC Observer)
Peter S. Nurczynski(Ernst & Young)
Debra MacLaughlin (BDO Seidman)
Tim Martin(McGladrey & Pullen)

II. BEST PRACTICES RELATING TO THE IMPLEMENTATION OF APPENDIX K OF THE SECPS RULES

There was a discussion on best practices. The Committee discussed best practices and the Task Force agreed that an article on best practices would be prepared for participation in a suitable medium.

III. ISSUES IN SWEDISH AUDIT REPORTS

It was noted that auditors reports in Sweden that were prepared in accordance with Swedish GAAS and company law referred to the auditor having responsibilities regarding the administration of the company and for determining whether the

directors should be discharged from their liability to the company.

The Task Force agreed that Joe Kelley would obtain further information as to the nature of the liabilities referred to by the auditors and whether these were merely liabilities relating to the obligation of the directors to prepare annual financial statements. If the latter was true, the task force did not believe there would be any US independence issues. The issue would be discussed further at the next meeting of the Task Force.

IV. STATUS OF PRIOR MINUTES

The AICPA web site contained minutes of meetings of the Task Force since 1996. Wayne Carnall had prepared a summary of issues discussed at meetings prior to that time, which were still current.

It was agreed this was a useful summary that should be added to the website.

It was also noted that Wayne was undertaking a more thorough analysis of all topics discussed by the Task Force with a view to preparing an index for inclusion on the website by country. This would be reviewed by the Task Force at the next meeting.

V. BRAZILIAN TAX ISSUES

At the November 2000 meeting, the Task Force had discussed the following issue. Because of the complexities of Brazilian tax law and the Brazilian constitution, as well as the long period of time required for final resolution of judicial proceedings, Brazilian corporate taxpayers frequently file lawsuits to attempt to overturn enacted tax law or suspend the effectiveness of the tax law. The accounting for these tax disputes has varied from company to company. As a result there is inconsistency as to whether companies are recording contingent gains or contingent losses for similar tax issues.

Four examples of the tax disputes in question are set out in Appendix A.

The Task Force noted that representatives of the multinational accounting firms in Brazil had discussed this issue. It was understood that they believed that since the IBRACON (the Brazilian Institute of Accountants) has a better first-hand knowledge of the tax laws and practices, the IBRACON should propose the framework for resolving this matter. IBRACON is addressing these matters under Brazilian GAAP. The representatives of the multinational accounting firms had therefore raised this topic with the IBRACON in the form of four questions.

For purposes of the US GAAP reconciliation, registrants must comply with FASB Statement 5 regarding contingent gains and losses. The Task Force will consider any conclusions reached by IBRACON in any future Task Force discussions regarding this matter. Certain Task Force members questioned whether Brazilian and US GAAP relating to contingencies, and tax contingencies in particular, are the same in all respects.

It was agreed that Joe Ossnoss would report further at the next meeting of the Task

Force.

VI. US GAAP INCOME STATEMENT AMOUNTS IN RECONCILED FINANCIAL STATEMENTS

Background

Item 17(c)(2)(ii) of Form 20-F requires for each balance sheet presented there should be a quantification of each material variation between an amount of a line item under primary GAAP and an amount under US GAAP. However, Item 17 only appears to require a reconciliation of net income. It does not appear to require the variation between line items in the income statement and the corresponding amount under US GAAP.

In Section VI.G of the International Financial Reporting and Disclosure Issues, the staff states that IAS 1 allows an enterprise to present an analysis of expenses using the classification based on either the nature of expenses or their function. The outline points out that the staff does not believe there is a difference in the application of the functional method under IAS and US GAAP and would therefore expect the same expense classification. The outline also notes that in cases where expenses are classified based on their nature, sufficient disclosure about functional expense classifications should be presented as part of the US GAAP reconciliation to provide an information content substantially similar to an income statement presentation under US GAAP and Regulation S-X.

Issue

To what extent does a foreign private issuer need to present US GAAP income statement amounts where the primary GAAP is non-US GAAP?

Discussion

The SEC staff made the following points:

Whether or not US GAAP income statement line items needed to be presented as part of the reconciliation was unaffected by whether or not the reconciliation was presented pursuant to Item 17 or Item 18.

The staff would not require presentation of US GAAP income statement amounts in all circumstances. For example, under local GAAP a lessee might account for a lease as an operating lease but under US GAAP as a capital lease. The staff would not require disclosure of total depreciation expense, total interest expense, and total lease expense on a US GAAP basis. But the reconciliation or notes thereto should quantify the effects on pre-tax income resulting from the difference for each of these components. Quantification of the components is also necessary to determine the classifications for the US GAAP balance sheet reconciliation.

In certain situations, certain US GAAP income statement line items might have a particular significance to users especially where the US GAAP measure gave a different impression, either in absolute or relative terms (i.e. impact on trends), from the local GAAP measure. The staff had therefore required, for example, in certain

circumstances that the registrant discloses operating income on a US GAAP basis.

Generally, the SEC staff took the view that where revenues on a local GAAP basis were materially different from a US GAAP basis they would likely require disclosure of the US GAAP revenues.

The staffs position in Section VI.G of the International Financial Reporting and Disclosure Issues did not necessarily require presentation of US GAAP income statement line items. A registrant could present a primary GAAP income statement based on expense nature classification and meet the staffs requirement by presenting a supplementary local GAAP income statement on the basis of functional expense classification.

VII. SELECTED FINANCIAL DATA

Background

The SEC Staff Training Manual says:

B. Selected Financial Data [Item 3A of revised Form 20-F]

1. Selected financial data should include amounts under U.S. GAAP, if different. The selected data should be provided for 5 years.

2. Selected data for the earliest two years of the five year period may be omitted if the registrant represents that the information cannot be provided without unreasonable effort or expense, and states the reasons for the omission in the filing.

Issue

Does selected financial data need to be presented for every line item specified by Item 3 of new Form 20-F where different under US GAAP from the primary GAAP.

Discussion

The SEC staff confirmed that if any amount required to be presented in selected financial data on a primary GAAP basis is different on a US GAAP basis, then the corresponding amount under US GAAP should also be shown.

This also applied to income from continuing operations even if that item was not presented under primary GAAP income, because primary GAAP had no distinction between continuing and discontinued operations.

VIII. COMPARATIVES FOR RULE 3-19(F)

Background

Section VIII.A of the Division of Corporation Finance's International Financial Reporting and Disclosure Issues (published on the SEC website and dated July 21,

2000) states:

"3-19(f) information does not trigger a requirement to include full interim financial statements more recent than otherwise required by Rule 3-19. For example, if complete financial statements related to the most recent quarter (but not the comparative period) is distributed in a foreign issuer's home country, that information must be included in the US registration statement. Comparative prior period information is not required because the information provided is included only because of 3-19(f). In order to avoid confusing US readers the registrants should include disclosure explaining why this information is provided particularly when the information is placed with other financial statements and may look incomplete. If the information provided contains a reconciliation to GAAP, the staff believes that inclusion of reconciled information for the prior periods generally will also be necessary to prevent the current period information for being misleading."

It is understood the staff applies the last sentence of this excerpt to mean that if a US GAAP reconciliation is included in the information provided pursuant to Rule 3-19(f), then comparatives (both in local GAAP and including a US GAAP reconciliation) have to be provided.

Issue

1. What is the rationale for the staffs interpretation of Rule 3-19(f)?

2. Are there any circumstances where although the information provided pursuant to Rule 3-19(f) includes a US GAAP reconciliation the SEC staff will not require that comparatives be presented?

3. Does other information in the filing (e.g., selected financial data, MD&A pro forma information) also need to be updated?

Discussion

4. The SEC staff said that the basis for Rule 3-19(f) was to ensure a level playing field. It ensured that if more recent information than would otherwise be required by the age of financial statement rules has been made available to investors in one jurisdiction, then that information should be made available to all investors. Equally, if a domestic registrant presented more recent information than that required by Rule 3-01 it would be required to present comparatives. A foreign private issuer is not ordinarily required to provide US GAAP information in its home jurisdiction. Accordingly, when a foreign private issuer presents more current US GAAP information, it effectively has decided to present interim financial statements, and is also required to present comparatives as required by Item 8.A.5 of new Form 20.F.

   The SEC staff also noted that in these circumstances the current and comparative interim period would need to be covered by MD&A and pro forma information would need to be updated to that date.

5. The SEC staff said that while they would consider a waiver in circumstances involving hardship, there were no general circumstances that would

automatically result in a waiver.

Generally, registrants should proceed on the basis that the staff would not waive the requirement for comparatives.

IX. PRO FORMA FINANCIAL STATEMENTS BY GERMAN FOREIGN PRIVATE ISSUERS NOT PREPARED IN ACCORDANCE WITH ARTICLE 11 OF REGULATION S-X

At its November 2000 meeting, the Task Force had concluded that the German pro forma practice for offerings on the German Neuer Markt was fundamentally different from US practice. Accountants would therefore need to be careful about association with such information. The Task Force agreed that when such pro forma was included in an offering document in the US, it should include:

- a description of the basis of preparation
- an explicit statement that the information did not comply with Article 11
- appropriate cautionary language about the usefulness of the information

The Task Force noted that the German profession was current reconsidering the form of the report that might be appropriate on pro forma financial statements that did not comply with Article 11. To the extent that the German profession modified the form of the report the Task Force would reconsider its views as to whether such reports could be included in offering documents in the US.

X. SEC TOPICS

0. Adoption of SAB 101

SAB 101 only addresses US GAAP. The staff has been asked whether it will challenge revenue recognition under the home-country GAAP if a registrant reports a SAB 101 adjustment in its US GAAP reconciliation. Absent indications of a serious deficiency, the staff would likely not challenge the revenue recognition practice under home-country GAAP.

Canadian registrants should be aware that the staff of the Ontario Securities Commission has published guidance regarding the implications of SAB 101 on revenue recognition under Canadian GAAP.

1. Errors and IAS

The SEC staff noted that IAS 8 permitted two treatments of fundamental errors; restatement of prior periods (benchmark) and correction in the current period income statement (permitted alternative). While both are acceptable under IAS, the staff noted that use of the permitted alternative would cause comparative periods to continue to be materially misstated. Accordingly, the permitted alternative treatment would not be acceptable in SEC filings. In response to Task Force questions, the staff indicated that it would also follow the same approach for registrants that report under home-country GAAP. If the primary GAAP required correction of an error in the current period income

statement without alternative, the issue should be discussed with the staff prior to filing.

2. Age of financial statements in a registration statement subject to Rule 512(a)(4) of Regulation S-K

The SEC staff noted that foreign private issuers must undertake to update their registration statements after the effective date as required by Item 512(a)(4) of Regulation S-K. Under that rule, a foreign private issuer must undertake (emphasis added):

. . . to file a post-effective amendment to the registration statement to include any financial statements required by Item 8.A. of Form 20-F at the start of any delayed offering or throughout a continuous offering. Financial statements and information otherwise required by Section 10(a)(3) of the Act need not be furnished, provided that the registrant includes in the prospectus, by means of a post-effective amendment, financial statements required pursuant to this paragraph (a)(4) and other information necessary to ensure that all other information in the prospectus is at least as current as the date of those financial statements. Notwithstanding the foregoing, with respect to registration statements on Form F-3, a post-effective amendment need not be filed to include financial statements and information required by Section 10(a)(3) of the Act or Rule 3-19 if such financial statements and information are contained in periodic reports filed with or furnished to the Commission by the registrant pursuant to section 13 or section 15(d) of the Securities Exchange Act of 1934 that are incorporated by reference in the Form F-3.

The SEC staff noted that this requirement was not presently discussed within the International Financial Reporting Issues Outline and would be covered in the next revision.

It was also noted that exchange offers in a Form F-4 for a previous 144a offering are considered to be a continuous offering and the financial statements need to be current during the offering period typically 30 days.

The SEC staff also noted that there was an error in the 2000 edition of the Division of Corporation Finances Accounting Disclosure Rules and Practices. This contained the following guidance regarding this matter (emphasis added):

Foreign private issuers are required to update the financial statements and other information included in a prospectus used more than nine months after effectiveness of a registration statement only when the financial statements would be as of a date later than the date of financial statements required under Item 8 of revised Form 20-F. Issuers filing on Form F-3 may incorporate by reference reports filed or furnished to the Commission that contain the updated financial statements rather than filing a post-effective amendment. [SK 512(a)(4)]

The SEC staff discussed the following example. A foreign private issuer with a December 31 year-end has a registration statement declared effective on

September 25, 2001. The registration statement covers the offering of securities to be offered on a continuous basis. The latest registrant financial statements included in the registration statement are the registrants audited financial statements as of and for the fiscal year ended December 31, 2000.

The SEC staff confirmed that Rule 512(a)(4) requires that a foreign private issuer would be required to update its financial statements as soon as they no longer meet the age of financial statements requirements of Item 8. Therefore, in the fact pattern outlined above, the registrant would be required to file unaudited financial statements for the six months ended June 30, 2001 on October 1, 2001.

3. Applicability of exemption in Form 20-F to not treat proportional consolidation as a reconciling item when the entity was not consolidated because of EITF 96-16

The SEC staff noted that Item 17/18(c) (2)(v) of Form 20-F permits a registrant whose local GAAP permits proportionate consolidation for investments in joint ventures that would be accounted for under the equity method under US GAAP to omit as a reconciling item differences in presentation provided certain strict conditions are met. The SEC staff noted that it was unlikely that an investment in an entity that under US GAAP was accounted for under the equity method pursuant to EITF 96-16 would meet the relevant conditions. For example, the existence of significant participating rights that preclude consolidation under EITF 96-16 would not ordinarily mean that all significant financial and operating policies of the entity are jointly controlled by all parties with an equity interest.

4. New Item 3 of Form 20-F

The SEC staff noted that new Item 3 of Form 20-F required within selected financial data certain per share measures such as income from operations, per share information that were not required by Statement of Financial Accounting Standards 128. The SEC staff noted that such measures need not be presented if they were not presented in the primary financial statements.

5. Confidential filings

The SEC staff announced that henceforth the confidential review process will be available only for IPOs or other initial registration statements or in other "extraordinary situations". Accordingly, foreign private issuers which have become reporting companies under the Securities Exchange Act of 1934 should expect that all registration statements will need to be publicly filed and include all necessary consents and all other appropriate signatures etc. Extraordinary situations should be discussed with the staff on a pre-filing basis.

XI. REPORTING CURRENCY FOR DOMESTIC ISSUERS WHICH ARE FOREIGN COMPANIES

Background

Rule 3-20 of regulation S-X gives a foreign private issuer flexibility in the determination of its reporting currency. What is less clear is whether a domestic issuer must use the US dollar as its reporting currency or whether it is possible to select another currency.

There are various references within the literature that are not consistent.

0. 1996 AICPA International Practices Task Force Discussion (see Appendix A)

   This guidance indicates that a domestic registrant may report in a currency other than the US dollar if (1) substantially all operations were in a single country (other than the US) and (2) the currency of that country was used as the reporting currency.

1. 2000 Staff Training Manual, Page 6-2 (see Appendix A)

   This guidance says that all foreign issuers that do not meet the definition of a foreign private issuer, other than Canadian companies, must report in US dollars. Canadian companies can report in Canadian dollars.

   This guidance seems inconsistent with the guidance given at the 1996 AICPA IPTF meeting because it does not provide an exception for foreign issuers who would meet the conditions stated in the 1996 IPTF guidance (i.e., substantially all operations in a single country outside the US).

2. 2000 Staff Training Manual, Page 6-18 (see Appendix A)

   This guidance implies that all domestic registrants may report in Euros. This would be inconsistent with both items of guidance discussed above.

3. 2000 International Issues Document on SEC's Web Site, Section VII. F. (see Appendix A)

   This guidance addresses US incorporated companies. It basically repeats the guidance from the 1996 AICPA IPTF meeting. It softens the requirements by permitting reporting in a currency other than the US dollar in situations where substantially all of a registrant's operations are conducted in a single functional currency (vs. country). However, it does not state whether it could be applied by foreign issuers that do not meet the definition of a foreign private issuer.

Issue

Are there any circumstances in which an entity that is not a foreign private issuer can use a currency other than the US dollar as its reporting currency?

Discussion

4. **Entities incorporated in the US.**

The SEC staff said that the International Financial Reporting and Disclosure Issues document (July 2000) set out the current position. Any domestic issuer may use a reporting currency other than the US dollar in situations where substantially all of its operations are conducted in a single functional currency (as opposed to conducted in a single country). The rationale for this is that if one particular currency is used to measure most transactions the financial statements would generally be more meaningful if that currency is used as the reporting currency.

The reference in the 2000 Training Manual to the use of the Euro by a domestic issuer was not intended to create the impression that all domestic registrants can report in Euros.

5. **Entities incorporated outside the US**

The SEC staff did not believe that it was appropriate to draw a distinction based on country of incorporation. The SEC staff position would therefore be the same as for domestic issuers incorporated in the US.

The SEC staff considered the following example. A registrant is incorporated in a country that is a member of the European Monetary Union and its functional currency is the Euro. It fails to meet the definition of being a foreign private issuer because more than 50% of its voting securities and directorships are held by US residents. It has the following profile:

6. More than 50% (but not substantially all) of the combined group revenues and more than 50% (but not substantially all) of net income arise in group entities where the functional currency is the Euro.
7. The US dollar is relatively insignificant as a functional currency for the group.
8. No other functional currency represents more than 20% of revenues or net income.

The SEC staff would ordinarily expect such an entity to use the US dollar as its reporting currency. Pre-clearance is recommended if a registrant intends to use any other reporting currency. In evaluating such a request, the staff would consider the extent to which past and future results would likely be subject to translation adjustments

XII. HYPERINFLATIONARY STATUS OF VENEZUELA

The hyperinflationary status of Venezuela had been discussed at the November 2000 meeting.

The rate of inflation continues to decline in Venezuela. At March 31, 2000, the cumulative three-year inflation rate is approximately 70%. The annual rate of inflation for 2000 was approximately 14% and the estimated rate in 2001 will be 15%. Economist are predicting an increasing rates of inflation in the future that will be attributable to:

- o Significant public spending
- o Increasing private consumption falling unemployment
- o Other Social reforms

The projected rates of inflation for the three years-ended 2004 are 19%, 25%, and 31%, respectively. Annual rates of approximately 26% will result in the three-year rate exceeding 100%.

As a member of OPEC, Venezuela is required to cut back on its oil production which will hurt the economy.

The Task Force concluded that, for all of the concerns expressed at the last Task Force meeting in November 2000, Venezuela should continue to be considered a highly inflationary economy. At the next Task Force meeting the issue will be re-evaluated. Absent unfavorable trends, it would be expected that Venezuela would no longer be considered a highly inflationary economy as of January 1, 2002.

XIII. APPLICABILITY OF SAS 50 TO FOREIGN AUDITOR FIRMS

Background

The SEC and the AICPA have rules that are designed to discourage opinion shopping. However, the Commissions rules regarding changes in auditors do not apply to foreign registrants. In addition, foreign firms may conclude that SAS 50 (AU 625) is not applicable to them since they are not members of the AICPA. However, the Commission has made it clear that the audits must be conducted in accordance with US GAAS.

Issues

Is SAS 50 applicable to foreign firms?

Discussion

The Task Force agreed that compliance with US GAAS included compliance with SAS 50. However, the Task Force needed to consider further the implications of concluding that an incoming successor auditor had not complied with SAS 50 and the degree to which the current issue was opinion shopping relating to US GAAP rather than local GAAP. The Task Force was comfortable with the conclusion that the SAS 50 requirements (including communication with present auditor) is applicable when the discussion relates to US GAAP and that Task Force members are encouraged to remind their networks of these requirements. There was less certainty with respect to communications related to local GAAP issues. Task Force members were asked to give this further consideration for our next meeting.

XIV. AUDITOR RESIGNATION

The SECPS rules require an accounting firm to notify the Chief Accountant of the Commission when they have resigned or have been terminated, etc. The objective of the direct reporting is to ensure that all changes in accountants are reported to the SEC. This information is matched with the 8-K filed by the company. Foreign issuers

do not file 8-Ks.

Item 304 of Regulation S-K regarding changes in auditors does not apply to foreign private issuers.

Issues

0. Even if 8-Ks are not filed, is it necessary to file a SECPS letter?
1. Should the Task Force recommend to the Commission that Item 304 of Regulation S-K regarding change in auditors apply to foreign private issuers?

Discussion

On Issue 1, the Task Force agreed it was not necessary to file a letter.

On Issue 2, the Task Force agreed that in 33 Act filings there is no reason for a distinction between a domestic and foreign private issuer although the arguments were not as strong in a 1934 environment. The Task Force agreed that the Chairman would discuss further with the SEC Practice Section to see if the SECPS supported the notion of encouraging the SEC to expand these requirements to foreign registrants.

XV. CONSENTS AND THE NEW FORM 20-F

Background

Item 10.G of new Form 20-F says:

STATEMENT BY EXPERTS. Where a statement or report attributed to a person as an expert is included in the document, provide such person's name, address and qualifications and a statement to the effect that such statement or report is included, in the form and context in which it is included, with the consent of that person, who has authorized the contents of that part of the document.

The instructions to Item 10 state:

0. In annual reports filed on Form 20-F:

   (a) You do not have to provide the information called for by Items 10.A, 10.F and 10.G; and

   (b) If the information called for by Item 10.B has been reported previously in a registration statement on Form 20-F or a registration statement filed under the Securities Act and has not changed, you may incorporate that information by a specific reference in the annual report to the previous registration statement.

   It is therefore clear that Item 10.G. of Form 20-F is not applicable when the form is used as an annual report.

Issue

When the Form 20-F is being used as a registration statement:

1. Is an audit report always considered a report by experts for purposes of this rule? Alternatively, must the filing specifically name the auditor as an expert for this requirement to apply?

2. Must the filing contain a consent from the accountant, or is it sufficient for the registrant to state in the filing that the report has been included with the consent of the accountant?

Discussion

The SEC staff noted that their intention was that when the new Form 20-F was used as a registration statement then a consent should be provided in exactly the same way as when a Form F-1 was used as a registration statement. In other words, a consent would always be required from the auditors and that consent would be included in the filing.

XVI. CONSENTS 40-F ANNUAL REPORT

Background

General instruction D of Form 40-F requires consent from the independent accountants in an annual report:

(10) If any accountant, engineer or appraiser or any person whose profession gives authority to a statement made by him, is named as having prepared or certified any part of the registration statement or annual report, or is named as having prepared or certified a report or valuation for use in connection with the registration statement or annual report, the manually signed, written consent of such person shall be filed.

Until the Commission amended Form 20-F as part of the new International Disclosure Standards, Commission rules did not require consents under the Securities Exchange Act of 1934 except for a 40-F.

Issues

0. Is consent required in an annual report on Form 40-F

1. Does a company need to comply with the staff policy that the consent must be dated within 30 days of filing?

Discussion

On Issue 1, the SEC staff said that consents should be filed.

On Issue 2, the SEC staff said that consent simply needs to be dated on or after the date of the audit report. Therefore, an accountant can sign the consent the same day as the audit opinion and the keeping current procedures would not be applicable

regardless of when the registrant filed the annual report.

XVII. COMPLIANCE IN JAPAN WITH AU 380 COMMUNICATIONS WITH AUDIT COMMITTEES

Background

The financial statements of foreign private issuers filed with the Securities and Exchange Commission are required to be audited in accordance with generally accepted auditing standards in the United States (US GAAP). This includes compliance with AU 380 Communications with Audit Committees. If a company does not have an audit committee, the independent accountants should satisfy the reporting requirements by communicating with the Board of Directors. This issue discusses how the accounting profession should comply with the communication requirements in the audit of a company in Japan.

Under the Japanese Commercial Code, all large companies are required to have a Board of Statutory Auditors of at least 3 members who have responsibility for the supervision of the audits, internal and external, of the company. In addition, the Boards of Directors of such companies also have responsibilities for the fair presentation of the financial statements prepared by such companies.

The membership of the boards of directors of Japanese corporations typically is comprised of senior members of management who are generally appointment by, and serve at the pleasure of, the Chief Executive Officer. It is extremely rare to have an independent director. While elected by the shareholders, the Board of Directors nominates the statutory auditors. Historically, the role of statutory auditor has been considered an honorary position and been filled by retired managers of the company, many from the accounting or finance function.

On March 28, 2001 the Japanese Ministry of Justice submitted a draft bill to the Corporate Law Subcommittee of the Judicial System Council containing broad amendments of the Commercial Code on corporate a management and audits, proposing the monitoring of corporate management and the abolishing of the existing statutory auditor system. The bill has been reportedly drafted in response to foreign investors complaints that the non-independence of the existing system could result in potential irregularities and accounting manipulations. Under the draft bill, if adopted, large corporations would be required to have at least one completely independent director. Those that have two or more such directors and establish committees on director nominations, compensation and audits in which independent directors comprise the majority of the committees will be able to discontinue the existing statutory auditor system. It is anticipated that this bill will not be presented to the Diet until at least next year which for practical purposes means that reform in this regard will unlikely to have taken effect until the fiscal year ending March 31, 2004 at the earliest.

Issue

Based on the existing structures, with whom should the auditor communicate those items required by AU 380?

Discussion

The Task Force agreed that communications required by AU380 should in the special circumstances of Japan be addressed in writing to both, the Board of Statutory Auditors and the Board of directors.

XVIII. RUSSIAN COMPANIES REPORTING IN US DOLLARS

Background

Effective July 1, 1992, the Russian government passed various laws and took other action to establish the convertibility of its currency, the Rouble. Prior to July 1, 1992, the Rouble did not float in relation to the US dollar and other currencies, and exchange rates were fixed by government action and were not intended to and did not represent market valuations. The official exchange rates were designed to capture and retain the very limited foreign currency entering the country. International trade was very limited and effectively, the Rouble was not convertible into US dollars or other currencies in any meaningful manner.

While currency restrictions still exist, there is a market within Russia for the conversion of Roubles into U.S. dollars and other foreign currencies, including the interbank currency exchange and over-the-counter and currency futures markets. However, at present there is not a market for conversion of Roubles into U.S. dollars or any other foreign currency outside of Russia and the other Commonwealth of Independent States (CIS).

The Russian economy is considered to be highly inflationary as defined by both Rule 3-20 of Regulation S-X and Statement of Financial Accounting Standard No. 52 Foreign Currency Translation (SFAS 52). Some Russian companies believe it is more appropriate to report in Roubles as that is the currency that is used to conduct business. These financial statements would be adjusted for the effects of inflation and presented in Roubles of equivalent purchasing power as of the balance sheet date. Other Russian companies believe that the US dollar is the most appropriate reporting currency because of its familiarity to investors outside of Russia. These financial statements remeasure amounts stated in Roubles into US dollars as if the US dollar was the functional currency.

Issue

Is it appropriate for a company whose currency of its primary economic environment is the Russian Rouble to report in US dollars in accordance with US GAAP in filings with the Commission?

Discussion

The Task Force agreed that a Russian entity could report in US Dollars.

XIX. DETERMINING THE CARRYING VALUE OF FIXED ASSETS OF RUSSIAN COMPANIES REPORTING IN US DOLLARS

The Task Force is presently considering the issue of determining how the carrying

value of fixed assets of Russian companies can be determined under US GAAP. When and if the Task Force concludes on the matter the issue summary and conclusion will be added to the minutes.

XX. CONVERSION FROM FOREIGN TO DOMESTIC ISSUER AND VISA VERSA

Background

Topic 6.I.B.2 in the SEC Staff Training Manual says:

A foreign issuer that loses its foreign private issuer status becomes subject to the reporting requirements for a domestic company on that date. While previous Exchange Act filings do not have to be amended upon the loss of foreign private issuers status, all future filings would be required to fully comply with the requirements for a domestic company. The financial statements and selected financial data should be recast into US GAAP and US dollar reporting currency for all periods presented.

Issues

0. When a foreign private issuer that loses its status and becomes a domestic issuer, when is the first periodic report on a domestic form due, and what financial statements must that report include?

1. What happens when a domestic issuer becomes a foreign private issuer?

2. Should a registrant report a change in a status on Form 8-K (or 6-K)?

Discussion

3. The SEC staff considered the following example. A foreign private issuer with a calendar year-end that loses its status as a foreign private issuer on May 1, 2000. The SEC staff said that the intention of the Training Manual that the first filing after failing the definition of a foreign private issuer would be for the quarter in which the issuer's status changed, i.e. the first 10-Q the registrant is required in the above fact pattern to file would be for the quarter ended June 30, 2000.

4. The SEC staff confirmed that the guidance in the Staff Training Manual relating to when an entity that was a foreign private issuer becomes a domestic issuer can be applied to the reverse situation. The Sec staff would also expect continuity of reporting. The SEC staff considered the following example. An entity that was previously a domestic issuer becomes a foreign private issuer on September 28, 2001. This would permit the company to begin 34 Act reporting as a foreign private issuer by ceasing to file 10-Qs and instead to file 6-Ks. Accordingly, absent any prior undertaking to security holders to provide quarterly information, it would not file a 10-Q for the quarter ended September 30, 2001. Its next filing (absent any information required to be communicated under cover of a Form 6-K) would be a Form 20-F due on June 30, 2002. If the change in status occurs before the due date for the 10-Q for the period ended September 30, 2001 but after the period end then the staff would expect it to file a 10Q for the period ended

September 30 2001.

5. The SEC staff thought it desirable, but not required, that changes in status should be communicated by filing Forms 8-K or Forms 6-K. when their status changes to communicate the change

XXI. MEXICAN TAX ISSUES

CIRCULAR 54

Background

Under Mexican GAAP and Mexican tax law, the basis of non-monetary assets and liabilities are adjusted for the effects of inflation. For financial reporting purposes, the basis of assets and liabilities is as of the balance sheet date, i.e. all amounts are expressed in a currency of equivalent purchasing power as of the balance sheet date. For tax purposes, the assets/liabilities reflect one-half of the rate of inflation in a given year.

To illustrate, assume an asset that is not depreciated was purchased for 1000 pesos on January 1, 2000. Inflation for the year was 15% and for the first six months was 8%. The carrying value in the financial statements at year-end was 1, 150 pesos. The tax basis at year-end would be 1,080 pesos only reflecting the effects of inflation through June 30. However, on January 1, 2001, the tax basis is increased to 1,150.

The Mexican Accounting Principles Commission recently issued Circular 54 that addresses the determination of temporary differences. Paragraph 3.8 states the following:

For the purposes of determining the temporary differences in assets and liabilities and calculating the related deferred income taxes, the book amounts should be compared to the bases of the tax amounts adjusted for inflation as of the date of the financial statements.

Accordingly, while the difference between the book basis and tax basis is 70, using the guidance in Circular 54, the basis of the tax amount would be adjusted to 1,150 pesos. As a result, there is no temporary difference.

Discussion

The Task Force concluded that while there is a difference in basis, it does not create a temporary difference as defined by SFAS 109 since it is impossible for it to result in a taxable or deductible amount in the subsequent year since it is adjusted on the first day of the subsequent year. Accordingly, a US GAAP reconciling difference will not be created as a result of Circular 54.

XXII. CLASSIFICATION OF THE MONETARY GAIN/LOSS ON DEFERRED TAX ASSET/LIABILITY

Background

Bulletin D-4 requires the monetary effect generated by the deferred tax asset or liability balance to be allocated between the tax provision or included as part of the integral result of financing: monetary gain/loss. The allocation is based on whether the item that gives rise to a temporary difference is a monetary or non-monetary item. If it is monetary, a monetary gain/loss will be recorded with an offsetting adjustment to income taxes. If the temporary difference is non-monetary, no monetary gain is recorded.

To illustrate this difference, the attached example from EITF 93-9 will be used. If the temporary difference were a non-monetary item, the company would record a tax expense of 10 pesos. If the temporary difference were monetary, the company would record a monetary gain of 50 pesos and a tax provision of 60 pesos. There is no difference in net income, but pretax income and tax expense will be different.

Note a to paragraph 96 of SFAS 89 states that Although classification of [deferred income taxes] as non-monetary may be technically preferable, the monetary classification provides a more practicable solution of the purposes of computing the purchasing power gain or loss on a consulted basis.

Issue

Is the method required by Bulletin D-4 acceptable under US GAAP?

Discussion

Yes. EITF 93-9 addressed how the liability and expense recognition should be determined. It did not address how the monetary effect should be allocated in the income statements. In a letter to the Mexican Accounting Principles Commission, the SEC staff indicated they would not object if the monetary gain/loss is allocated to the tax provision thereby effectively treating deferred taxes as non-monetary or not allocated to the tax premium. The staff did indicate that the method used should be described.

This conclusion is conceptually consistent with paragraph 230 of SFAS 109 in which the foreign exchange gain/loss from remeasurement of the deferred tax liability or asset can be recorded as part of the tax provision or included with other foreign exchange gains/losses.

To facilitate a comparison of companies on a pretax basis, Mexican companies should disclose the amount of monetary gain/loss that is included in pretax profits.

Next Meeting

The next meeting of the Task Force is scheduled for November 20, 2001.

Appendix A

Examples of Brazilian Tax Issues

1. IPI Tax - Credits for taxes presumed paid on purchases of tax-exempt goods to be

used in the production of goods subject to tax

The IPI (Imposto sobre Productos Industrializados) is a federal value-added tax. Each company in the production chain is entitled to take a credit for the IPI included in its purchased inputs into the production process, which can then be offset against the IPI payable on its sales. In recent years taxpayers have begun to claim that they are entitled to a "presumed credit" for the IPI that would have been payable on purchases which, for various reasons, have been exempted from IPI.

In one case, the Supreme Court established a legal precedent in accepting that a presumed credit could be taken for the IPI that would have been payable had their purchases of concentrate, from their production facility in the Manaus Free Trade Zone, not been exempted from tax. However, in Brazil, such Supreme Court decisions are not required to be applied to all similar or even identical cases. Therefore, this decision is not applicable to other cases of the same type. No other decisions have been reached to date.

The applicable law is silent with respect to presumed credits. One attorney might say that the tax is unconstitutional, and another might say that the law is silent on this issue. Both might say that it is probable that their clients would prevail in court. If a company takes the presumed credit against taxes due on sales of their product, is this considered to be the recording of a gain contingency, or is it considered to be an aggressive position?

2. ICMS Credits on Purchase of Fixed Assets and Non-productive Material

The ICMS (Imposto sobre Circulao de Mercadorias e Servios) is a state value-added tax. In October 1996, a change in ICMS regulations established that credits could be taken on purchases of fixed assets used exclusively in the productive process. Prior to this change, purchasers of fixed assets would pay the tax as an end user. Some companies have initiated legal actions challenging that the same treatment should apply for ICMS credits on these fixed asset purchases made before October 1996. These credits would be applied against the ICMS payable on the company's sales. In some cases, companies have obtained court orders, which permit them to claim and use the credits. These court orders are subject to reversal in the higher courts.

One attorney might say that the tax is unconstitutional, and another might say that the law is silent on this issue. Both might say that it is probable that their clients would prevail in court. If a company takes the presumed credit against taxes due on sales of their product, is this considered to be the recording of a gain contingency, or is it considered to be an aggressive position?

3. Calculation Basis for the PIS Tax

The PIS (Programa de Integrao Social) is a Federal tax on gross revenues. In 1988, two Decree Laws[1] established that the PIS calculation basis (i.e., gross revenues) should be indexed to inflation between the date of the sale and the date of the tax payment, and also increased the rate of the tax. Several companies challenged the legitimacy of the two Decree Laws in the courts, alleging that they were unconstitutional. The Federal Supreme Court eventually declared that the Decree Laws could not alter the calculation basis of a Constitutional Law, and a 1995 Senate resolution[2] extended the Supreme Courts decision to all taxpayers, effectively

overturning the Decree Laws. Some companies have been claiming for refunds for PIS taxes paid during the period from 1988 to 1995. Given the very high rates of inflation in Brazil until1995, the amounts claimed have been significant.

The tax authorities have asserted that the actions by the Supreme Court and the Senate affected only the definition of the calculation basis, but did not affect the definition of the indexation procedure in the Decree Laws. Recent decisions at the level of the Superior Court[3] have been inconsistent, and the Supreme Court may eventually overturn these decisions. In the tax courts, the decisions have been favourable to the taxpayers, and the tax authorities are no longer issuing assessments in connection with this issue.

4. Summer Plan implementation

In 1994, the "Summer Plan" was implemented by the Federal Government, in the form of a series of Decree Laws, to attempt to combat excessive inflation. Before the implementation, the government, on a monthly basis, issued the monetary correction figures for the past month to be utilized to calculate tax effects of inflation, which allowed companies to monetarily correct their tax deductions. At the implementation of the Summer Plan, the government skipped one month of inflation by implementing the new plan with a month delay after expiration of the old plan. Many companies argued for the recovery of this lost monetary correction. Given the amount of inflation at the time of the skipped month, the amounts involved are significant. Some companies have taken deductions for this, with or without court injunctions, and others have not. There have been no Supreme Court rulings on this issue. Most attorneys believe the legal arguments for a refund are strong. However, the amount involved may be too large for the government to allow Companies to win.

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[1] A Decree Law is a law issued by the President. It can be renewed an unlimited number of times by the President, but it is considered temporary. Decree laws become constitutional only if the Congress passes them as regular laws.

[2] If approved by the President, or his veto is overridden, a Senate resolution is final, in that it changes the constitution.

[3] The Superior Court is an appellate court below the Supreme Court.