SEC REGULATIONS COMMITTEE
Joint Meeting with SEC Staff
June 11, 2002
SEC Headquarters - Washington, D.C.

HIGHLIGHTS

NOTICE: The AICPA SEC Regulations Committee 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

A. SEC Regulations Committee

Jay Hartig
David Follet
John Gerdener
Wendy Hambleton
Chris Holmes
Gary Illiano
Jim Ledwith
Scott Pohlman
Sam Ranzilla
Roy Van Brunt
Leonard Weinstock
John Wolfson

B. Securities and Exchange Commission

Office of the Chief Accountant

Robert Herdman, Chief Accountant
Jack Albert, Associate Chief Accountant
Cathy Cole, Associate Chief Accountant
Shelly Luisi, Associate Chief Accountant

Division of Corporation Finance

Carol Stacey, Chief Accountant
Craig Olinger, Deputy Chief Accountant
Todd Hardiman, Associate Chief Accountant
Joel Levine, Associate Chief Accountant
Leslie Overton, Associate Chief Accountant

Division of Enforcement

Charles Niemeier, Chief Accountant

C. AICPA

Annette Schumacher Barr

II. PERSONNEL CHANGES

Mr. Herdman noted that four new Professional Accounting Fellows will begin their two-year term in the Office of the Chief Accountant: Douglas D. Alkema, Eric J. Schuppenhauer, Gregory A. Faucette and Randolph P. Green. Deputy Chief Accountant John Morrissey has left the Commission. The Deputy Chief Accountant position will be posted in an effort to find a replacement.

III. STATUS UPDATES

The staff provided a status update on the following initiatives:

A. Accelerated Filing Proposed Rulemaking

Carol Stacey noted that the staff has received over 300 comment letters responding to its proposal to accelerate filing deadlines for periodic reports. The responses received vary. Some respondents stated that the shorter filing periods are attainable while others state that such deadlines will not be accomplished without a sacrifice in reporting quality. Some respondents stated that the shorter reporting periods were feasible for10-Ks but not for10-Qs while other letters stated the opposite. A number of comment letters offered various alternatives to the staff's proposal, such as linking reporting due dates to press releases. The staff is in the process of summarizing the comments received, with the goal of issuing a final rule by the end of the year.

B. Critical Accounting Policies

The staff noted that the proposed rulemaking was issued on May 10 and comments are due July 19. Jay Hartig stated that the Committee has formed a task force to draft the Committee's response to the proposal.

C. Supplemental Financial Information Proposal

Mr. Herdman noted that the Critical Accounting Policy proposal may obviate the need to finalize this proposal. As such, there is no current timetable for finalization.

D. Pending 8-K and Management Certification Proposals

At its open meeting on June 12, the Commission will discuss proposals to 1) revise Form 8-K and 2) require management certification of quarterly and annual reports. *[Note: The proposals were issued June 17. Comments on the 8-K Proposal were due August 26; Comments on the Certification Proposal were due August 19. A final rule requiring management to certify the financial and other information contained in a company's quarterly and annual reports as well as to provide a certification regarding the company's disclosure controls was effective on August 29. (Release No. 33-8124)]*

Due to postal safety precautions that have caused delays in mail deliveries, the staff recommends the use of electronic mail, fax or private overnight delivery when submitting comment letters and other non-EDGAR correspondence.

E. Staff Review of Fortune 500 10-K Filings

The staff completed its screening of Fortune 500 10-K filings in May. The staff will continue to screen non-calendar-year-end companies and June year-end companies this summer. Carol Stacey noted that these reviews should not impact the routine reporting procedures for most registrants.

F. Enforcement Update

Charles Niemeier highlighted the following areas of concern that have come to the attention to his staff:

- ✓ Top-side adjustments for which there is inadequate documentation or support.
- ✓ Transactions which have no business purpose, usually involving parties that have colluded in some way. The staff has recently seen these types of transactions in the telecommunications, energy and internet industries. He stated that although these transactions may be structured in a way that complies with GAAP, they are misleading to investors. The staff expects full and fair disclosure of these transactions and the impact they have on the financial operations of the company.

Mr. Niemeier added that the Enron collapse has heightened investor attention to liquidity and cash flow from operations. Because SFAS No. 95 provides a certain amount of flexibility, the staff is concerned there is a risk that certain manipulations may occur in the reporting of cash flows.

IV. PRACTICE ISSUES

A. Transitional Disclosures under Statement 142, *Goodwill and Other Intangible Assets*

Topic. Questions have arisen regarding the application of the transitional disclosures required by paragraph 61 of FAS 142 to previously issued annual financial statements included or incorporated by reference in a proxy statement or registration statement.

Question. Should previously issued annual financial statements that are included in a proxy statement or registration statement be revised to include the transitional disclosures described in paragraph 61 of FAS 142 if the proxy statement or registration statement also includes interim financial statements which reflect the initial application of FAS 142? Would the conclusion be different if the previously issued annual financial statements are incorporated by reference rather than included?

Background.

Paragraph 61 of FAS 142 indicates that:

> *"In the period of initial application and thereafter until goodwill and all other intangible assets have been accounted for in accordance with this Statement in all periods presented, the following information shall be displayed either on the face of the income statement or in the notes to the financial statements: income before extraordinary items and net income for all periods presented adjusted to exclude amortization expense (including any related tax effects) recognized in those periods related to goodwill, intangible assets that are no longer being amortized, any deferred credit related to an excess over cost (amortized in accordance with Opinion 16), and equity method goodwill. The adjusted income before extraordinary items and net income also shall reflect any adjustments for changes in amortization periods for intangible assets that will continue to be amortized as a result of initially applying this Statement (including any related tax effects). In addition, the notes to the financial statements shall disclose a reconciliation of reported net income to the adjusted net income. Similarly adjusted earnings-per-share amounts for all periods presented may be presented either on the face of the income statement or in the notes to the financial statements."*

For the year in which FAS 142 is adopted, a registrant is required to include in each of its Form 10-Q filings for that year the above-described transitional disclosures with respect to each quarterly and year-to-date period for the corresponding period of the preceding year. In its Form 10-K for the year in which FAS 142 is adopted, the registrant would need to include the paragraph 61 transitional disclosures for each of the two preceding years. Application of the transitional guidance is required if the amounts involved are material.

SEC Staff Position.

If previously issued annual financial statements are reproduced in connection with a proxy statement or registration statement subsequent to the issuance of interim financial information reflecting the initial adoption of FAS 142, the annual financial statements would need to be revised to include the paragraph 61 transitional disclosures, if the amounts involved are material. This view is based on paragraph 61, which indicates that "in the period of initial application" adjusted net income and per share information should be displayed "for all periods presented… either on the face of the income statement or in the notes to the financial statements."

DCF is deferring to the registrant and its auditors the assessment as to whether GAAP requires the transitional disclosures of SFAS 142 to be included in the most recent annual financial statements that are being reissued via incorporation by reference (i.e., NOT reproduced) into a proxy statement or registration statement that also incorporates by reference interim financial statements reflecting the initial adoption of SFAS 142. Firms should decide for themselves whether they can permit reissuance of their opinion without restatement in this circumstance. However, if restated financial statements are not filed (under cover of Form 8-K, Item 5, for example) then the registration statement or proxy statement must prominently present at least, selected financial data (even though not required by instructions to the registration statement or proxy statement) that includes the transitional disclosures required by SFAS 142.

Therefore, DCF would allow for flexibility in how registrants satisfy the disclosure requirements of SFAS 142, which might be by:

1. Including the transitional disclosures in the proxy statement or registration statement (note that data for only the three most recent years and interim periods would suffice, even if the transitional disclosures are included in a five-year table).

2. Filing the transitional disclosures in an 8-K that is incorporated by reference into the proxy statement or registration statement.

3. Including the information in a Form 10-Q that is incorporated by reference into the proxy statement or registration statement.

Irrespective of the method a registrant chooses for providing the transitional disclosures, the disclosures should be robust and transparent and should cover all periods for which financial statements are presented. The disclosures should include (or cross reference to) the date that SFAS 142 was adopted, a brief description of the standard, a discussion of the impact that adoption has had on the financial statements, and a discussion of the paragraph 61 disclosures. Also, if the registrant has not completed its transitional goodwill impairment testing, it should include a discussion as to its status and related uncertainties.

This position is similar to DCF's position regarding the adoption of SFAS 128 subsequent to a Form 10-K that is incorporated by reference into a registration statement or proxy statement. DCF's position is predicated on an expectation that the auditor will consent to incorporation of its report on the annual financial statements only after assuring that the transitional disclosure required by SFAS 142 is complete and correct.

B. Timeliness of Financial Statements in 1933 Act Registration Statements for Issuers that have changed year-end

Topic: Timeliness of Financial Statements in 1933 Act Registration Statements for Issuers that have changed year-end.

Question: A registrant changes its year-end to a date that results in a transition period of less than six months. The registrant files a transition report on Form 10-Q containing unaudited financial statements for the transition period. In connection with a 1933 Act registration statement, when must the transition period be audited?

For example, assume a registrant files a Form 10-K for the year ended September 30, 2001. On December 1, 2001 the registrant changes its year-end to December 31 and files a transition report on Form 10-Q containing unaudited financial statements for the three months ended December 31, 2001. In connection with a 1933 Act registration statement, when must the financial statements for the three months ended December 31, 2001 be audited?

Background: The SEC Training Manual has the following guidance:

Even if an issuer complies with Exchange Act requirements following an election to change the fiscal year, it may be required to provide more current audited financial statements in a Securities Act registration statement by the form's instructions.

Under Rule 3-12 of Regulation S-X audited financial statements must be presented either 45 or 90 days after year-end as required by paragraph (c) of Rule 3-01 of Regulation S-X.

Discussion:

View A – The new year end is December 31, 2001. Audited financial statements for the three months ended December 31, 2001 must be presented 90 days after December 31, 2001.

View B – The three month period ended December 31, 2001 does not constitute a year. The most recent year is September 30, 2001. Audited financial statements for the three months ended December 31, 2001 must be presented either one year and 45 days after September 30, 2001 or one year and 90 days after September 30, 2001 depending on compliance with paragraph (c) of Rule 3-01 of Regulation S-X.

View C – Upon the required filing date for the December 31, 2002 financial statements, which would be either 45 or 90 days after such year-end date depending on where the registrant stood under S-X 3-01(c), provide the audited financial statements for both the three-month and twelve month periods. (i.e., Span of time since last audited statements could approach 18 months in total.)

Conclusion:

Carol Stacey stated that View B reflects the staff's current view.