

**SEC Regulations Committee  
June 23, 2009 - Joint Meeting with SEC Staff  
SEC Offices – Washington DC**

**HIGHLIGHTS**

**NOTICE:** The Center for Audit Quality (CAQ) SEC Regulations Committee meets periodically with the staff of the SEC to discuss emerging financial 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. The highlights do not represent official positions of the CAQ. As with all other documents issued by the CAQ, these highlights are not authoritative.

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As available on this website, Highlights of Joint Meetings of the SEC Regulations Committee and its International Practices Task Force (IPTF) and the SEC staff are not updated for the subsequent issuance of technical pronouncements or positions taken by the SEC staff, nor are they deleted when they are superseded by the issuance of subsequent highlights or authoritative accounting or auditing literature.

**I. ATTENDANCE**

**A. SEC Regulations Committee**

Chris Holmes, Chair  
Melanie Dolan, Vice Chair  
Doug Bennett  
Leonard Brams  
Michael Cinalli  
Brad Davidson  
Christine Davine  
Karin French  
Len Gatti  
Bob Laux  
Jeff Lenz  
Scott Pohlman  
Amy Ripepi  
Tom Weirich

Kurtis Wolff  
John Wolfson

**B. Securities and Exchange Commission**

*Division of Corporation Finance*

Wayne Carnall, Chief Accountant  
Craig Olinger, Deputy Chief Accountant  
Mark Kronforst, Deputy Chief Accountant  
Angela Crane, Associate Chief Accountant  
Jill Davis, Associate Chief Accountant  
Michael Fay, Associate Chief Accountant  
Stephanie Hunsaker, Associate Chief Accountant  
Steven Jacobs, Associate Chief Accountant  
Leslie Overton, Associate Chief Accountant  
Greg Burton, Academic Fellow  
Michael Stehlik, Staff Accountant  
Mark Green, Senior Special Counsel

*Office of the Chief Accountant*

Shelly Luisi, Associate Chief Accountant

**C. Center for Audit Quality**

Annette Schumacher Barr

**D. Guests**

Mark Barton, E&Y  
John May, PwC

**II. DIVISION OF CORPORATION FINANCE UPDATE**

**A. Personnel Update**

Wayne Carnall addressed recent promotions in the Division of Corporation Finance:

- **Angela Crane** was appointed as an Associate Chief Accountant. She will work with Deputy Chief Accountant Mark Kronforst in the new policy group. Ms. Crane joined the Division of Corporation Finance in June 2000, and most recently was a Branch Chief in the Office of Electronics and Machinery.

- **Jill Davis** was appointed as an Associate Chief Accountant. She will work with Deputy Chief Accountant Craig Olinger in the operations group. Ms. Davis joined the Division of Corporation Finance in September 1997, and most recently was a Branch Chief in the Office of Natural Resources.

Mr. Carnall also announced that **Stephanie Hunsaker** was the winner of the Andrew Barr Award.

## **B. Financial Reporting Manual**

Mr. Carnall indicated that an update to the Division's Financial Reporting Manual (FRM) is expected to be published in mid-July. Mr. Carnall stated that the most significant change will be the addition of Topic 4, "Independent Accountants' Involvement." Mr. Carnall also stated that the SEC staff is in the process of reviewing staff positions discussed in previous joint meetings of the Committee and the SEC staff to determine if they should be included in the FRM. He anticipates that this project will be completed by December 2009.

## **C. IFRS**

In connection with the reviews of foreign private issuers that prepare their financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board the staff is evaluating how it can best assess the consistency of the interpretation and application of IFRS across jurisdictions.

# **III. CURRENT FINANCIAL REPORTING MATTERS**

Mr. Carnall commented on the following reporting issues that have been noted during the SEC staff's review of 2008 year-end filings and 2009 interim filings:

## **A. Goodwill and Long-Lived Asset Impairment**

Mr. Carnall observed that, although many registrants have provided voluminous disclosures regarding goodwill impairment within the critical accounting policy section of Management's Discussion and Analysis, it is not always clear how the information is meaningful to investors. Further, registrants have tended to provide disclosures that appear to focus on the non-cash nature of the goodwill impairment charge to the exclusion of the business and economic conditions that gave rise to the charge. SEC staff comment letters have requested disclosures in Management's Discussion and Analysis that describe impairment testing and the future implications to the registrant's business of the conditions that resulted in impairments. Mr. Carnall stated that the SEC staff is considering providing informal

guidance in the near-term to provide registrants with a better understanding of its expectations in this area.

**B. Deferred Tax Asset Valuation Allowances**

The SEC staff may ask registrants that have recorded a goodwill impairment whether or not they also have considered the implications of the conditions that resulted in the impairment on any deferred tax assets.

**C. Recent FASB Standards - Other than Temporary Impairment of Debt Securities and Fair Value Measures in Inactive Markets**

Stephanie Hunsaker provided observations about the disclosures made by early adopters of FASB Staff Position FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments* (FSP FAS 115-2), and FASB Staff Position FAS 157- 4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability has Significantly Decreased and Identifying Transactions that are Not Orderly* (FSP FAS 157-4).

With respect to FSP FAS 157-4, Ms. Hunsaker commented that most early adopters stated that the FSP did not have a significant effect on their financial statements. Accordingly, the SEC staff has not issued many comments in this area.

With respect to FSP FAS 115-2, the SEC staff has issued a number of comments to early adopters. The majority of SEC staff comments involve the income statement presentation of total OTTI, the portion recognized in OCI, and the portion recognized in earnings. There have been several different presentations which are acceptable including:

- presenting all the amounts within the income statement.
- presenting the gross OTTI and the OCI portion parenthetically within the OTTI caption on the face of the income statement (registrants should avoid presentations that are too wordy or lengthy in periods where comparative disclosures are required.)
- presenting the disclosure separately at the bottom of the income statement.
- presenting the disclosure only in the notes to the financial statements, which Ms. Hunsaker stated would be acceptable only if the OTTI amounts are clearly immaterial.

The SEC staff also has issued a number of comments relating to the measurement of the portion of OTTI related to credit losses. In connection with those comments, they requested additional disclosure relating to the inputs and assumptions by major security type. Ms.

Hunsaker stated that it may be more informative to provide those disclosures using a weighted average (rather than disclosing a range in which the minimum and maximum vary significantly). In some cases, the SEC staff has taken exception to a registrant's assumptions (e.g., a current valuation of pooled trust preferred securities that assumes a non-exercise of call provisions, whereas the previous valuation assumed exercise of the calls at the first call date, without sufficient evidence to support the change in assumption, resulting in a substantially higher estimate of fair value of the security tranche held by the registrant). The staff has also questioned whether security types are being properly identified and the existence of concentrations below general categories.

**D. Fair Value Measures**

Many registrants adopted the fair value measure requirements of FAS 157/ASC Topic 820 for non-financial items (e.g. goodwill and long-lived assets) in the first quarter of 2009. However, not all registrants provided the related required disclosures in their first quarter financial statements with respect to fair value measurements relating to non-financial assets and non-financial liabilities. Mr. Carnall reminded the Committee of this disclosure requirement.

**IV. IMPLEMENTATION AND INTERPRETATION OF RECENT SEC RELEASES**

**A. Technical Amendments to Regulations S-K and S-X**

Mr. Carnall commented that the objective of the SEC's recent technical amendments to Regulations S-X and S-K was to conform to FASB Statement 141(R), *Business Combinations* (Statement 141(R)) and FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements* (Statement 160). The SEC did not intend to make any substantive changes to the computations required by the amended rules (e.g., significance tests, ratio of earnings to fixed charges). However, the SEC staff is aware of a few editorial errors within the amendments that will be corrected in the future.

**B. Reporting on Internal Controls over Financial Reporting by Non-Accelerated Filers**

Mr. Carnall declined to comment whether the SEC will grant an additional extension of the auditor attestation requirement under Section 404(b) for non-accelerated filers. He noted that unless the SEC takes action, Section 404(b) will become effective for non-accelerated filers for fiscal years ending on or after December 15, 2009. Mr. Carnall noted that in Release No. 33-8934A, the SEC recently extended the expiration date of two

temporary rules through June 30, 2010. However, this technical correction does not affect the effective date for compliance by a non-accelerated filer with Section 404(b).

### **C. XBRL**

Mark Green noted that the SEC staff's recently issued Compliance and Disclosure Interpretations (C&DI's) on interactive data address certain implementation issues faced by registrants. In response to a Committee member's question related to the process for releasing updated taxonomies, Mr. Green stated that currently there is no set plan for the timing and frequency of the SEC's approval for use of updates to the XBRL US GAAP taxonomy.

When the 2009 US GAAP taxonomy is approved for use later in 2009, the SEC encourages its use as soon as possible. Due to the timing of the approval, however, issuers will be permitted to use the 2008 US GAAP taxonomy for an interim period.

Committee members noted that uncertainties regarding updates to the XBRL taxonomy and related SEC compliance requirements were causing some companies to outsource XBRL tagging, at least during the initial phase-in periods. Further, the late availability of the 2009 taxonomy was causing registrants to use the 2008 taxonomy with company-specific extensions for GAAP line items not addressed in the 2008 release. Committee members expressed concern that this might dilute the benefit of XBRL to issuers.

## **V. NEW OR PENDING ACCOUNTING STANDARDS AND PRONOUNCEMENTS**

### **A. Reporting retrospective accounting changes in a Form 10-K/A filed to correct an error in prior period annual financial statements**

At the September 2003 SEC Regulations Committee Joint Meeting with the SEC staff, the SEC staff stated that a Form 10-K/A filed to correct an error in prior period annual financial statements should not reflect the subsequent events which will require retrospective treatment in future reports (e.g., retrospective application of a new accounting principle, discontinued operations, change in segments). However, the Committee noted that there is diversity in practice, with some companies including the effects of these accounting changes in the amended Form 10-K and others presenting the retrospective effects of the accounting changes in a Form 8-K. Further adding to the confusion is the upcoming implementation of the FASB standard on

subsequent events (FAS 165/ASC Topic 855) and the requirement to dual date for subsequent events in reissued financial statements.

Mr. Carnall confirmed the correction of a material error in prior period financial statements should be reported via an amendment to the previously filed Form 10-K (i.e., a Form 10-K/A). Corrections of material errors should not be reported using Form 8-K. Further, corrections of material errors should be filed as timely as possible.

Mr. Carnall indicated that the SEC staff has changed its perspective from that conveyed at the September 2003 meeting. The SEC staff believes that once a company files interim information that requires retrospective treatment that any subsequent amendment to Form 10-K to correct an error should reflect the retrospective accounting. To illustrate, assume the company adopts a new accounting standard that requires retrospective application in the first quarter that is reflected in the Form 10-Q. If the company subsequently discovers an error in prior year financial statements, the amended financial statements should reflect BOTH the retrospective application of the new accounting standard AND the correction of error. The disclosures should clearly segregate these two items. This filing should be on Form 10-K/A vs. Form 8-K.

Mr. Carnall continued that this change should not result in a delay in filing a Form 10-K/A for an error correction. For example, if a calendar year company discovered an error in early April before it filed its 10-Q it should not delay filing the Form 10-K/A for which the Company could determine the impact until after the filing of the Form 10-Q.

## **B. Redeemable equity classified outside of permanent equity**

Under the FASB's new statement on noncontrolling interests, registrants are required to reconcile total equity at the beginning of the period to total equity at the end of the period (See paragraph 38(c) of ARB 51, as amended by FAS 160/ASC Topic 810-10-50-1A(c)). The SEC's recent technical amendments to S-X Rule 3-04, similarly require registrants to reconcile *total equity* at the beginning of the period to *total equity* at the end of the period. However, the SEC rules continue to prohibit including redeemable equity in any caption titled "total equity." (See Financial Reporting Release (FRR) Section 211). While redeemable equity is not permanent equity, it is nevertheless equity. Therefore, the SEC staff noted that registrants should present it in the reconciliation provided to comply with Statement 160. However, registrants with redeemable noncontrolling interests, redeemable preferred stock or other redeemable equity classified outside permanent equity should not include these items in any total or subtotal caption titled "total equity". The renaming of the caption in the statement of changes in shareholders' equity "total

equity” to “total” does not make the inclusion of redeemable equity acceptable.

Mr. Carnall explained that the reason this is not an acceptable means of presentation is that it would be including something in total equity that is not shareholders’ equity.

Mr. Carnall expressed concern that, in their first quarter financial statements, some registrants presented a reconciliation that included redeemable equity in total equity which is inconsistent with FRR 211. Mr. Carnall expects those registrants to change the presentation in their second quarter filings.

Mr. Carnall identified two acceptable means of presentation to satisfy the requirements of both SEC’s rules and GAAP:

- Provide a column for redeemable noncontrolling interests in the equity reconciliation, but exclude the related amounts from any “total” column. In that case, the reconciliation could include a row for net income or a supplemental table identifying the allocation of net income among controlling interests, nonredeemable noncontrolling interests and redeemable noncontrolling interests.
- Exclude redeemable noncontrolling interests from the equity reconciliation, but provide a supplemental table (e.g., in the notes to the financial statements or the “statement of changes in equity and noncontrolling interests”) reconciling the beginning and ending balance of redeemable noncontrolling interests. In that case, the caption “net income” in the equity reconciliation could note parenthetically the amounts related to redeemable noncontrolling interests.

### **C. Push-Down Accounting after Adopting the FASB’s New Standard on Noncontrolling Interests (FAS 160/ASC Topic 810-10-55/65)**

The SEC staff recently released SEC Staff Accounting Bulletin (SAB) No. 112 to update various SABs for recent changes in GAAP. One such update relates to SAB Topic 5J on push down accounting. The SEC staff noted that the principle in push down accounting remains unchanged: to reflect the parent’s basis in the subsidiary on the subsidiary’s financial statements. Accordingly, the staff confirmed the application of SAB Topic 5J, as revised by SAB 112, in the following fact patterns:

- Company A purchases between 80% and 95% of Company B and elects push down accounting. In that case, 100% of Company B’s fair value (and thus 100% of any goodwill resulting from the new basis of accounting



recorded by Company A) should be pushed down in Company B's separate financial statements. This is because SAB Topic 5J requires Company B's financial statements to reflect the new basis of accounting recorded by Company A upon acquisition.

- Company A acquires substantially all of Company B in a series of transactions. Consistent with the requirements of FASB Statement No. 141R, Company A reflects the acquisition of Company B at 100% of its fair value as of the date on which control is obtained. For example, assume Company A purchases 25% of Company B in March 2009, an additional 35% interest in September 2010 and the remaining 40% interest in June 2012. Company A will report its acquisition of Company B at fair value in September 2010 at the time the additional 35% interest (i.e., control) is obtained; the June 2012 purchase of the 40% noncontrolling interest represents an equity transaction that does not affect Company A's basis in Company B. In that case, in June 2012, at which point Company B became 100% owned and push down accounting would be required, the amount pushed down in Company B's separate financial statements is the amount that Company A recorded in the transaction which resulted in control (September 2010 in this example).

**D. Information required in registration statements when there are retrospective adjustments to provisional amounts after adoption of the FASB's new standard on business combinations (FAS 141R/ASC Topic 805)**

Under the FASB's new business combination standard, adjustments to provisional allocations of purchase price during the measurement period result in retrospective changes to prior financial statements. At the April 9, 2008 SEC Regulations Committee Joint Meeting with the SEC staff (see Discussion Document A.7), the SEC staff stated that when a material retrospective adjustment to provisional amounts is required and the adjustment has not yet been reflected in subsequent financial statements, the registrant must provide revised financial statements reflecting that material retrospective adjustment prior effectiveness of a registration statement (other than Form S-8).

These circumstances differ from those in which a revision of historical financial statements is required as a result of an accounting change (e.g., discontinued operations, change in reporting segments, retrospective accounting changes). In those cases, revised audited financial statements are not required (or permitted) until the registrant has filed interim financial statements reflecting the subsequent accounting change.

Mr. Carnall confirmed the SEC staff's previously expressed view and noted that this information will be incorporated into a future version of the FRM. Mr. Carnall also confirmed that, in the absence of a registration statement, a

registrant could file a Form 8-K to voluntarily provide financial statements reflecting a material retrospective adjustment to the provisional amounts previously reported.

## **E. FASB Codification**

For annual and interim periods ending after September 15, 2009, the FASB Accounting Standards Codification (the “Codification”) will become the single source of authoritative generally accepted accounting principles (GAAP) in the United States.

Mr. Carnall discussed financial statement references once the FASB Codification becomes effective. Mr. Carnall encouraged companies to make financial statements more useful to users by drafting financial statement disclosures to avoid specific GAAP references and to more clearly explain accounting concepts.

If references to specific GAAP are made in financial statements for periods ending on or before September 15, 2009 (i.e., before the Codification becomes effective) the SEC staff believes pre-Codification GAAP references continue to be acceptable, even if those financial statements were issued after September 15, 2009 (e.g., in a Form 10-K or Form 10-Q for the annual or quarterly period ended August 31, 2009). Further, the SEC staff will not object if those financial statements refer to either the Codification or both the Codification and pre-Codification GAAP literature.

Once a company issues financial statements for a period ending after September 15, 2009 the SEC staff believes any references to specific elements of GAAP should use Codification references. That is, if references to specific GAAP are made in financial statements for periods ending after September 15, 2009 (e.g., annual or interim financial statements as of September 30, 2009), those references should be to the Codification. Moreover, references to specific GAAP throughout the financial statements should be on a consistent basis for all periods (i.e., disclosures for comparative periods should not refer to only pre-Codification GAAP literature).

After the Codification becomes effective, the SEC staff does not expect companies to revise or amend financial statements previously filed for prior periods simply because financial statements for periods ending after September 15, 2009 refer to the Codification. That is, a company’s December 31, 2008 Form 10-K, with references to only pre-Codification GAAP literature, may be incorporated by reference into a Form S-3 registration statement that becomes effective after September 15, 2009, even if the Form S-3 also incorporates by reference the September 30, 2009 Form 10-Q that refers to the Codification.

The Codification includes relevant portions of authoritative content issued by the SEC and the SEC staff for reference by public companies. The inclusion of the SEC content is intended to increase the utility of the Codification for public companies who file with the SEC. The Codification does not replace the specific rules and interpretive releases of the SEC or its staff and does not change the SEC content. The Codification should not change practice with respect to any references to specific SEC rules and interpretive releases in financial statements.

The SEC staff will not require a preferability letter if an accounting change is in response to a newly issued update of the Codification.

## **VI. CURRENT PRACTICE ISSUES**

### **A. Predecessor Financial Statements**

Guidance in section 1140.7 of the FRM and Release No. 33-8587, *Use of Form S-8, Form 8-K, and Form 20-F by Shell Companies*, states that after consummation of a transaction between a nonreporting operating company and a public shell company (registrant) that is accounted for as a recapitalization of the operating company, the registrant must file a Form 8-K providing audited financial statements of the operating company, which will replace the shell's historical financial statements (as predecessor of the registrant) in future filings.

The FRM does not specifically address the circumstance in which a public shell company acquires an operating company in a transaction that is not accounted for as a recapitalization or a reverse acquisition. An example would be the purchase of an operating company by a special purpose acquisition company (SPAC). In those circumstances, while financial statements of the acquired company are provided in a Form 8-K in connection with the acquisition, the Committee believes there is currently diversity regarding whether the pre-acquisition financial statements of the operating company must be provided in the registrant's annual and quarterly reports.

Mr. Carnall indicated that designation of a predecessor is usually required if a public company succeeds to substantially all of the business of the operating company and the registrant's own operations prior to the succession appear insignificant relative to the operations assumed or acquired. That is, when a public shell company acquires an operating company and accounts for the transaction as a business combination, the acquired business is likely a predecessor for which pre-acquisition financial statements should be presented, in all SEC filings and for all periods required, in addition to the pre- and post-acquisition financial statements of the registrant.

## **B. Reconsideration Events for Variable Interest Entities**

An Item 2.01 Form 8-K is required when a “registrant or any of its majority-owned subsidiaries has completed the acquisition or disposition of a significant amount of assets, otherwise than in the ordinary course of business....”

Instruction 2 to Item 2.01 defines acquisitions to include “acquisition by lease, exchange, merger, consolidation, succession or other acquisition.” Accordingly, when a registrant concludes that it must consolidate a variable interest entity (VIE) as a result of a reconsideration event under FIN 46(R)/ASC Topic 810-10-35 that makes the registrant the entity’s primary beneficiary, the registrant should consider whether the consolidation meets the significance thresholds for reporting under Item 2.01 of Form 8-K, even if the registrant did not issue any consideration.

The Item 2.01 Form 8-K reporting thresholds and requirements vary based on whether or not the VIE represents a business under Regulation S-X Rule 11-01(d). If the VIE is a business and significant, the Item 2.01 Form 8-K must include S-X Rule 3-05 financial statements under Item 9.01 of Form 8-K, as well as pro forma financial information under S-X Article 11.

Committee members discussed the timing requirement of the Form 8-K, whether it must be filed within four business days of the FIN 46(R) reconsideration event, and the implications to a registrant’s eligibility to use Form S-3. In many cases, it might be difficult for a registrant to meet a four day reporting deadline, because it might only identify a reconsideration event during the interim or annual financial reporting closing process. The Committee discussed using the date the registrant files financial statements reflecting consolidation of the VIE as the Form 8-K triggering event, rather than the date of the FIN 46(R) reconsideration event. The SEC staff indicated that they have not reached a conclusion at this time and would give further consideration to this question.