

# AcSEC UPDATE

A publication of the Accounting Standards Executive Committee  
and the Accounting Standards Team of the AICPA

In June 2007, AcSEC issued Statement of Position (SOP) 07-1, *Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies*.

On February 14, 2008, the FASB issued FASB Staff Position (FSP) 07-1-1. The FSP delays indefinitely the effective date of SOP 07-1. Entities that early adopted SOP 07-1 before December 15, 2007 are permitted, but not required, to continue to apply the provisions of the SOP. No other entities may adopt the provision of the SOP, subject to the exception: If a parent entity that early adopted the SOP chooses not to rescind its early adoption, an entity consolidated by the parent entity that is formed or acquired after that parent entity's adoption of the SOP must apply the provisions of the SOP in its stand-alone financial statements. For a copy of the FSP, visit the FASB's website at [http://www.fasb.org/pdf/fsp\\_sop07-1-1.pdf](http://www.fasb.org/pdf/fsp_sop07-1-1.pdf).

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## AcSEC COMMENT LETTERS

On May 30, 2008, the Accounting Standards Executive Committee (AcSEC) provided comments on the FASB Preliminary Views Document, *Financial Instruments with Characteristics of Equity*.

On April 15, 2008, the Planning Subcommittee (PSC) of the Accounting Standards Executive Committee (AcSEC) of the American Institute of Certified Public Accountants offered its comments on the FASB's Exposure Draft of a proposed FASB Staff Position, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures*.

On January 17, 2007, AcSEC shared thoughts on how FASB issues its standards, and in particular, proposed that FASB should develop a policy of having all newly issued major standards go effective at a set date in a given year.

On January 16, 2008, AcSEC issued a comment letter on the FASB's Exposure Draft of a proposed FASB Staff Position FAS 142-f, *Determination of the Useful Life of Intangible Assets*.

On January 15, 2008, AICPA provided comments on the Governmental Accounting Standards Board (GASB) Exposure Draft (ED), *Accounting and Financial Reporting for Derivative Instruments*.

To view full text of these comment letters, please visit <http://www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+Standards/comltrs/index.htm>

## CURRENT AcSEC PROJECTS

AcSEC participates in updating the following AICPA Guides.

### **Airline Audit and Accounting Guide**

**Description and Background.** The AICPA Audit and Accounting Guide *Audits of Airlines* (the Airline Guide) was originally issued in 1981. The Airline Guide has not been revised or amended, other than for conforming changes, since its issuance. In 1981, the airline industry in the U.S. had recently been deregulated and the top 10 U.S. airlines carried substantially all domestic passengers. Since 1981, more than 100 airlines have

filed for bankruptcy protection. And today low-cost and regional airlines, which were just in their infancy at the time the Airline Guide was originally written, enjoy considerable market share. In addition, carriers have been affected by a number of unprecedented crippling events, including, among other things, the terrorist attacks of September 11, 2001, and resulting closure of the entire U.S. airspace for several days thereafter. Key pieces of the strategy on which the major carriers based their businesses after airline deregulation have become risky and unworkable.

Also, a number of new arrangements and transactions have emerged over the years in the airline industry, which are not addressed in the Airline Guide. Frequent flyer programs that began in the 1980s currently represent between 5 and 10 percent of an airline's total revenue passenger miles and have contributed to significant revenue from other entities that pay for access to airline customer lists and trade names. In the maintenance and engineering arena, although historically most major airlines performed maintenance on their own aircraft in-house, now many airlines outsource some or all of the scheduled maintenance activities under power-by-the-hour contracts (PBTH contracts) or have maintenance joint ventures with independent maintenance and repair entities.

The industry events described above have resulted in substantial changes to the operations of airlines, which in turn have led to the emergence of many new accounting and auditing issues. Many of the accounting issues have led to diversity in practice. Furthermore, the industry background section of the Airline Guide needs to be updated to reflect the significant developments since 1981.

In 2002, a task force began work on a project to revise the Airline Guide.

***Current developments and plans.*** On September 12, 2007, AcSEC issued an exposure draft of a proposed revised Audit and Accounting Guide, *Airlines*. The proposed revised Guide addresses many new accounting issues that have emerged over the years. It also includes chapters dedicated specifically to air cargo and regional carriers. The comment period ended on December 15, 2007. The exposure draft and the related comment letters are posted to the AICPA Web site on the following page <http://www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+Standards/Exposure+Draft+of+Proposed+Audit+and+Accounting+Guide+-+Airlines.htm>.

At March 2008 AcSEC meeting, the Airline Task Force discussed with AcSEC how to address certain comments received in connection with the exposure draft.

At May 2008 meeting, AcSEC discussed revisions made to the proposed Audit and Accounting Guide, *Airlines*, to address comments received in connection with the Guide exposure draft. AcSEC suggested a number of clarifications to the Guide.

At May 2008 meeting, AcSEC voted to approve the Guide for final issuance (except for the deferred revenue section) subject to its negative clearance. With respect to the

deferred revenue section, which was also discussed at this meeting, AcSEC suggested a number of revisions and clarifications to this section. The Airline Task Force plans to revise this section and to bring it back to AcSEC in July. If AcSEC approves this section in July, then at that point the entire accounting portion of the guide will be cleared for issuance as final.

Staff: Yelena Mishkevich

## **Casino Audit and Accounting Guide**

**Description and background.** The AICPA Audit and Accounting Guide *Audits of Casinos* (the Casino Guide) was originally issued in 1984. The Casino Guide has not been revised or amended, other than for conforming changes, since its issuance. The casino industry and its financial reporting have changed since 1984. Casinos have experienced a shift in their primary revenue source from table games to slot machines; slot machine technology has evolved, for example, competing casinos participate together in progressive slots; and some regulators' positions and views about jackpot liabilities have changed. Also, the industry has grown and expanded to new jurisdictions. Some of these changes have resulted in accounting and auditing issues not contemplated in the existing Casino Guide. Many of the accounting issues have led to diversity in practice. Further, diversity in practice exists in applying certain accounting standards issued since 1984.

In 2003, a task force began work on a project to revise the Casino Guide.

**Tentative conclusions.** Some of the tentative conclusions reached by AcSEC in discussing the Casino Guide are as follows:

- **Scope – transactions and entities covered.** The Casino Guide should address accounting issues of casinos, including issues arising from transactions that typically are unique to entities undertaking gambling activities. In addition, the scope of the Casino Guide should be transaction based. Therefore, to the extent that entities other than those that traditionally may have been considered casinos undertake gambling and related activities that are the same as gambling and related activities undertaken by casinos, as well as other gambling and related activities, the activities of those other entities should be subject to the guidance in the Casino Guide. To better describe the kinds of activities covered by the Casino Guide, the Guide would likely be retitled *Audits of Casinos and Other Gaming Activities* or something similar.

The FASB has on its agenda a project to address recognition of revenue and liabilities in financial statements. This Casino Guide project is not intended to address issues that may overlap with issues addressed in the FASB's project.

- *Scope – Native American entity undertaking gambling activities.* The Casino Guide should apply to entities owned by state and local governments that undertake gambling activities, such as Native American casinos. The Casino Guide should include guidance for those entities electing post-1989 FASB pronouncements as well as those not electing post-1989 FASB pronouncements. The Casino Guide should therefore have three tracks: (1) FASB entities that undertake gambling activities; (2) state and local governments electing post-1989 FASB pronouncements that undertake gambling activities; and (3) state and local governments not electing post-1989 FASB pronouncements that undertake gambling activities.
- *Impairment of long-lived assets and restructuring charges.* The Casino Guide should reiterate the requirements of category (a) GAAP, separately identifying those that are limited to FASB entities, GASB entities, and SEC registrants. Also, the Casino Guide should include industry-specific illustrations of typical impairment and restructuring transactions and activities and how they might be reported in applying those pronouncements to entities undertaking gambling activities, such as illustrations addressing asset groupings and triggering events. Those illustrations would be intended to provide guidance for specific fact patterns though not necessarily explicit requirements or prohibitions.
- *Jackpot liability.* The Casino Guide should provide that entities undertaking gambling activities should accrue jackpot liabilities only for amounts the entity is legally obligated to pay as of the reporting date. The primary example of amounts operators are obligated to pay is the incremental portion of progressive jackpots in circumstances in which the operator is prohibited from removing the machine from the floor without transferring the incremental progressive liability to other machines or games.
- *Loan guarantees.* For state and local governments electing post-1989 FASB pronouncements and undertaking gambling activities, FASB Interpretation (FIN) No. 45, *Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, provides guidance on accounting for guarantees and elaborates on the disclosures to be made by a guarantor about its obligations under certain guarantees that it has issued. The Casino Guide should provide additional guidance, perhaps through illustrations, on the application of FIN No. 45 to entities undertaking gambling activities.
- *Incentive programs.* Incentives to play should be bifurcated and characterized as either (a) marketing incentives to induce potential customers to enter into transactions or (b) loyalty programs for customers, based on activities or transactions undertaken. At its September 2005 meeting, AcSEC agreed that the Casino Guide should—
  - Describe current practice, including a (1) deferred revenue model and (2) a model in which an entity reports the full amount of the original revenue transaction and

accrues liabilities under loyalty or incentive programs for costs associated with rewarding the customers undertaking those original revenue transactions (referred to for the time being as an *immediate revenue* model).

- Describe the basis for each model and provide that in practice the deferred revenue model is acceptable in virtually all circumstances, while the immediate revenue model is acceptable only in certain circumstances. For example, an immediate revenue model is unacceptable in circumstances in which (a) a significant number of paying customers are being displaced by customers redeeming awards or (b) the value of an individual award is significant as compared with the purchase earning the award.
  - Provide detailed guidance on applying appropriate EITF and other relevant literature, such as EITF Issue No. 01-9, “Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products),” to those models, including guidance applicable to cash and free play awards. Consider what disclosures, if any, should be considered in connection with loyalty programs. The scope and provisions of any guidance in these areas should continue to be coordinated with AcSEC's project to revise the AICPA Audit and Accounting Guide *Audits of Airlines*.
- *Participation arrangements – revenue vs. expense (display)*. AcSEC asked the task force to consider whether participation arrangements may be leases in conformity with EITF Issue No. 01-8, “Determining Whether an Arrangement Contains a Lease.” For participation arrangements that are leases, entities should follow lease accounting. For participation arrangements that are not leases, entities should consider the guidance in EITF Issue No. 99-19, “Reporting Revenue Gross as a Principal versus Net as an Agent.” The Casino Guide should include illustrations of typical participation arrangements and how they might be reported.

Also, the Casino Guide should note that activities of all parties undertaking participation arrangements would be subject to the provisions of the Casino Guide to the extent that those activities are within the scope of the Casino Guide. For example, a slot machine manufacturer and owner undertaking a participation arrangement with an entity undertaking gambling activities is effectively undertaking gambling activities itself and therefore would be subject to the provisions of the Casino Guide pertaining to participation arrangements.

- *Classification of complimentaries (display)*. Expenses for complimentaries should be reported at cost (no revenue should be reported as a result of providing complimentaries). In circumstances in which customers have the choice of receiving either complimentaries or free play, expenses should reported as the estimated cost of complimentaries to be provided (with free play presumed to have no cost). The expenses should be classified in the department they benefit, which typically is the casino department.

- *Payments or commitments to make payments to not-for-profit organizations (or other entities) in connection with obtaining the right to manage properties for third parties.* Such payments or commitments are exchange transactions, rather than contributions. Payments made as part of efforts to acquire agreements should be expensed as incurred. Also, such payments made pursuant to an existing agreement should be capitalized and amortized over the life of the agreement, without anticipating potential renewals.
- *Gaming license and market entry costs.* Gaming licenses typically, though not in all cases, have indefinite lives. Determining the life of a license may require judgment, including considering the nature of the renewal process and additional economic sacrifices, if any, required to renew the license. License and related market entry costs incurred in anticipation of obtaining a license should be expensed as incurred. License and related market entry costs incurred after it is probable that a license will be acquired should be capitalized. In circumstances in which licenses have indefinite lives, those capitalized costs should be assessed for impairment every year. In circumstances in which the licenses have finite lives, those capitalized costs should be amortized over the life of the license. Also, the revised Casino Guide should include examples of factors that may affect the value of the license, such as a jurisdiction issuing a large number of licenses in subsequent years, thereby diluting the value of existing licenses.
- *Gaming taxes.* Gaming taxes are not income taxes. Gaming taxes paid based on graduated rates should be reported in interim periods based on the expected average rates. AcSEC also requested the task force to further consider the following issues to be discussed at a future AcSEC meeting:
  - Whether international convergence issues exist.
  - The effect of rate changes (other than changes based on graduated rates already in place). In particular, consider how and in what period to account for the change. AcSEC asked the task force to research analogous GAAP pertaining to this issue.
- *Customer credit policy.* For SEC registrants, the Casino Guide should reiterate the SEC Management Discussion and Analysis requirements pertaining to changes in customer credit policy.
- *Free cash flows.* For SEC registrants, the Casino Guide should reiterate that SEC Financial Reporting Release No. 65, *Conditions for Use of Non-GAAP Financial Measures*, provides, among other things, that public companies that disclose or release such non-GAAP financial measures include in that disclosure or release a presentation of the most directly comparable GAAP financial measure; a reconciliation of the disclosed non-GAAP financial measure to the most directly comparable GAAP financial measure; and a statement explaining why the entity

believes that that non-GAAP financial measure provides useful information to investors regarding the registrant's financial condition and results of operations.

- *Segment reporting.* AcSEC agreed to defer further discussion of this issue pending the outcome of a potential FASB FSP and EITF consensus on related issues. In the meantime, AcSEC agreed that the conforming change in the current Casino Guide should be more robust in tracking the guidance in FASB Statement No. 131, *Disclosures about Segments of an Enterprise and Related Information*.
- *Illustrative financial statements.* The Casino Guide should include illustrative financial statements for FASB casinos and for GASB casinos, including Native American casinos.

### ***Current developments and plans.***

At its March 19, 2008 meeting, AcSEC discussed the following drafts of the proposed Gaming Industry Audit and Accounting Guide: Chapters 1, "Industry Overview," 2, "Guide Scope and Applicability," 3, "Overview of Gaming and Gaming Related Revenue," 4, "Jackpot Liabilities," 5, "Participation and Similar Arrangements," 6, "Loyalty and Incentive Programs," 7, "Gaming License, Project Development and Preopening and Start-up Costs," 8, "Managing Properties for Third Parties," 9, "Guarantees," 10, "Long-Lived Assets," 11, "Other Accounting Topics," and 12, "Governmental Gaming Entities" along with Appendixes A, "Illustrative Financial Statements," B, "Illustrative Guidance when Accounting for Guarantees," C, "The New Jersey Casino Reinvestment Development Authority (CRDA)," D, "Currency Transaction Reporting in the Gaming Industry," E, "Rules of the Games," and F, "Glossary." During the March 19, 2008 meeting, AcSEC approved the proposed Guide for exposure, subject to negative clearance.

AcSEC plans to expose the Guide in 2008.

Staff: Renee Rampulla, Rampulla Advisory Services, LLC (consultant)

### **Health Care Audit and Accounting Guide**

***Description and Background.*** The AICPA Audit and Accounting Guide *Health Care Organizations* (the HC Guide) was originally issued in 1996. Substantial industry changes have resulted in the emergence of many new accounting and auditing issues, as well as the need to revise the industry background section of the HC Guide. Many of the accounting issues have led to diversity in practice.

In 2004, a task force began work on a project to revise the HC Guide.

***Tentative conclusions.*** Some of the tentative conclusions reached by AcSEC are as follows:

- ***Charity care:***
  - Charity care does not include services provided under contracts with third-party payors (such as Medicare or Medicaid) for payments that are less than the “full” amounts billable under the provider’s rate schedule.
  - The determination as to whether an individual meets the criteria for charity care typically should occur as soon as practicable, and before any substantial collection effort is initiated.
  - Disclosures on the level of charity care should include, at a minimum, a disclosure based on the health care organization’s *costs* of providing charity care. If other measures of the level of charity care such as the provider’s rates are disclosed as well, additional details should be included as to the source of those measures and how they are determined.
  - It is recommended that a health care organization disclose information on its various categories (individually and in total) of the broader metric of uncompensated care other than bad debts.
  
- ***Medical malpractice.*** With respect to recognition and measurement of medical malpractice and other insurance-related liabilities, and related disclosures, the HC Guide will direct health care organizations to the relevant guidance in FASB Statement No. 5, *Accounting for Contingencies*, and FASB Interpretation No. 14, *Reasonable Estimation of the Amount of a Loss: an interpretation of FASB Statement No. 5*. In determining “best estimates” of accrued liabilities under FASB Statement No. 5, health care organizations should take into consideration how claims develop over time—for example, the fact that some claims require a number of years before they are settled.
  
- ***Revenue recognition.*** Currently, notably in the case of self-pay patients, there is diversity in practice such that, following paragraph 5.03 of the HC Guide, some health care organizations may record revenue and an allowance (which may be relatively large) without necessarily determining first whether collectibility is reasonably assured. At its November 15-16, 2005 meeting, AcSEC reviewed chapter 10, “Revenues, Expenses, Gains, and Losses,” of the proposed revised HC Guide and recommended that the principle that collectibility should be reasonably assured before revenue may be recognized be applied to health care organizations. In addition, those health care entities that are SEC registrants should consider revenue recognition guidelines found in SEC Staff Accounting Bulletin No. 104, *Revenue Recognition*.
  
- ***Settlements.*** It is recommended that health care organizations disclose summaries of period settlement activity for significant governmental and other third-party payor

payables and receivables. In so doing, health care organizations should be mindful of the disclosure requirements of SOP 94-6, *Disclosure of Certain Significant Risks and Uncertainties*, related to changes in estimate for settlements. At its November 2005 meeting, AcSEC agreed that disclosures proposed by the task force for settlement activity should be included in the illustrative financial statements of the revised HC Guide.

- *Loss contracts.* In determining whether a health care organization should recognize a loss when it is probable that expected health care and maintenance costs under a group of existing contracts will exceed anticipated future premiums and stop-loss insurance recoveries on those contracts, only incremental costs should be considered.
- *Prepaid health care – classification of revenue.* Under typical prepaid health care services arrangements—for example, health maintenance organizations (HMOs)—revenue earned relates to both the assumption of medical risk and the providing of administrative services. Under such arrangements, administrative services are typically an integral part of providing or arranging medical care. That is, the HMO performs administrative services in support of its primary obligation to provide or arrange medical care (rather than for another party, as is the case in administrative-services-only (ASO) arrangements). Revenue relating to such administrative services should not be bifurcated from premium revenue related to the assumption of medical risk but should rather be included in premium revenue.
- *Prepaid health care – reporting of receivables and payables related to administrative-services-only (ASO) contracts.* Health care organizations should look to the terms of the contracts to determine the parties’ respective obligations and should apply FASB Interpretation No. 39 (FIN 39), *Offsetting of Amounts Related to Certain Contracts*. Under FIN 39, a right of setoff exists only if certain conditions are met, and typically those conditions are not met in situations involving more than two parties. Because a typical ASO arrangement involves three parties (the employer, the hospital or other provider of health care to employees, and the ASO organization), typically receivables and payables related to ASO contracts are reported gross.
- *Prepaid health care – capitation arrangements.* Capitation costs for a health care organization should not be reported analogously to reinsurance arrangements, that is, as premiums ceded that reduce premium revenue, but rather should be reported as an expense.
- *Gross versus net presentation of insurance claims and related insurance recoverables.* Currently, the HC Guide is scoped out from the requirement under FIN 39 (as interpreted by EITF Issue No. 03-8, “Accounting for Claims-Made Insurance and Retroactive Insurance Contracts by the Insured Entity”) to, in general, not offset prepaid insurance and expected insurance recoverables against related insurance

liabilities. The HC Guide currently permits offsetting, which is also current industry practice. AcSEC voted to recommend to the FASB that the HC Guide be amended such that there would no longer be an exception to FIN 39 for health care organizations.

- *Income statement classification and disclosure of gains and losses from nonhedging derivatives.* AcSEC discussed “economic hedges,” that is, derivatives entered into by an entity to hedge a specific exposure but that do not meet all of the conditions for hedge accounting treatment under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. AcSEC agreed (14 to 0) that the HC Guide should recommend that a not-for-profit health care organization disclose both the amounts of gains and losses relating to economic hedges and the specific line items (above the performance indicator) in which those gains and losses appear. AcSEC agreed that the HC Guide should not provide guidance about classification of gains and losses (e.g., a realized component included in the determination of “interest expense” that facilitates determining the effectiveness of the hedge, and an unrealized component included as a mark-to-market adjustment to nonoperating income [but above the performance indicator]).
- *Accounting for transfers between unrelated not-for-profit healthcare organizations.* AcSEC agreed with the task force that equity transactions or transfers between unrelated not-for-profit healthcare organizations should be recorded as contributions at fair value, with the transferor recognizing the contribution made as expense in the period made and as a decrease of assets or increase of liabilities, depending on the form of the benefits given, pursuant to paragraph 18 of FASB Statement No. 116, *Accounting for Contributions Received and Contributions Made*. The transferee would record the net assets at fair value at the transfer date. AcSEC also discussed the financial statement presentation of the contributions made by not-for-profit healthcare organizations. AcSEC concluded that contributions should be presented within the performance indicator in the financial statements of the transferor. AcSEC concluded that chapter 10 of the HC Guide should also address the financial statement presentation of contributions received.
- *Accounting for intercompany receivables when collection is doubtful.* The HC Guide Revision Task Force requested that AcSEC consider the issue of accounting for intercompany receivables when collection is doubtful, as currently there is diversity in practice in the accounting and reporting for such receivables. Currently, paragraph 11.26 of the HC Guide states that “if the receivable is not to be repaid, or if the receiving entity is perceived as unable to repay, it [write-off of intercompany receivable] may be accounted for as an equity transfer with the transferor reducing net assets and the transferee increasing net assets at the date such determination is made.” AcSEC recommended clarifying the wording in paragraph 11.26 of the HC Guide to state that accounting for write-offs of intercompany receivables as equity transfers is

not a free choice. Similarly to footnote 1 of APB Opinion No. 26, *Early Extinguishment of Debt*, paragraph 11.26 is intended to remind accountants to examine the facts and circumstances of each individual transaction to determine whether it is in substance a loss or an equity transfer. AcSEC further stated that the HC Guide should provide additional examples to assist practitioners in assessing the substance of these transactions.

- *Accounting for joint operating agreements.* The Healthcare Guide Revision Task Force requested that AcSEC consider the issue of accounting for joint operating agreements (JOAs). A JOA generally consists of two or more not-for-profit health care organizations (HCOs) entering into an agreement whereby the parties jointly operate and control certain of their hospitals or facilities while sharing the operating results and residual interest upon dissolution based on an agreed-upon ratio or ratios. There is currently diversity in practice in the accounting and reporting for joint operating agreements, as HCOs account for JOAs either by consolidating, using the equity method, at cost (e.g., risk sharing with a management agreement), or by using proportional consolidation. AcSEC agreed with the task force that chapter 11 of the HC Guide should incorporate guidance from Technical Practice Aid 6400.33, *Accounting for a Joint Operating Agreement*, and include more explicit guidance to address the variance in practice that currently exists.
- *Accounting for transfers involving goodwill between for-profit healthcare organizations and not-for-profit healthcare organizations where one healthcare organization controls the other or they are under common control.* AcSEC requested that the task force expand the analysis to include other examples of transfers that may occur between for-profit healthcare organizations and not-for-profit healthcare organizations where one healthcare organization controls the other or they are under common control and relevant accounting literature that may provide guidance for other kinds of such transfers. The task force agreed to broaden the issue and present it to AcSEC at a future meeting.
- *Accounting for pooled investments.* AcSEC expressed a preference to apply the same beneficial interest accounting in a financially interrelated scenario as in the non-financially interrelated scenario, versus the alternative of the HCO having a free choice between that accounting method and a method similar to the equity method under APB 18.

***Current developments and plans.*** At the March 2008 AcSEC meeting, the Health Care Guide Task Force discussed three chapters with AcSEC: Chapter 5, “Derivatives”; Chapter 9, “Contingencies and Other Liabilities”; and Chapter 16, “Unique Considerations of State and Local Government Health Care Organizations.”

The Task Force had previously discussed Chapter 5 with AcSEC and updated the chapter based on the recommendations AcSEC made. Following discussion of the chapter, AcSEC cleared the chapter.

The Task Force presented a discussion document for Chapter 9. The Task Force sought clarification regarding the accounting for certain transactions involving contingencies. Based on the recommendation of AcSEC, the Task Force will revise the chapter and present it to AcSEC at a future meeting.

The Task Force presented Chapter 16. This is a new chapter, combining the guidance for governmental health care organizations into one new, consolidated chapter. Following discussion of the chapter, AcSEC cleared the chapter.

Currently, AcSEC plans to expose the Guide in 2008.

Staff: Zachary Donahue

## **Employee Benefit Plans Audit and Accounting Guide**

***Description and Background.*** The AICPA Audit and Accounting Guide *Employee Benefit Plans* was last issued in 1991. The Guide has not been revised or amended, other than for conforming changes, since then. (There were two editions of the Guide prior to the 1991 edition: a 1983 edition and a 1988 edition.) Since 1991, significant changes have occurred in the types of retirement plans offered by employers, the way plans are administered, and the types of investments plans are holding. Many of these changes have resulted in accounting issues not contemplated in the existing Guide.

In 2004 a task force began work on a project to revise the employee benefit plans (EBP) Guide.

***Tentative conclusions.*** Some of the tentative conclusions reached by AcSEC in discussing the EBP Guide are as follows:

- *Accounting for contributions receivable for defined benefit pension plans.* Minimum contributions required should be accrued, and any excess amounts would be considered a Type II subsequent event unless there was evidence of a formal commitment as of the balance sheet date. When the issue is drafted for the EBP Guide, it should be expanded to discuss all of the factors listed in paragraph 10 of FASB Statement No. 35, *Accounting and Reporting by Defined Benefit Pension Plans*, with emphasis placed on the formal commitment.
- *Accounting for contributions receivable for defined contribution pension plans.* Additional guidance should be included in the EBP Guide discussing factors that

should be reviewed in determining whether contributions should be recorded due to an obligation resulting from a formal commitment under paragraph 10 of FASB Statement No. 35, and additional information about the relationship between employees and employer as compared with defined benefit plans.

- *Accounting for contributions receivable for defined benefit health and welfare benefit plans.* A receivable from the employer should be accrued equal to the liability for employees' claims recorded prior to the plan's year-end. For claims incurred-but-not-reported (IBNR), a receivable from the employer should be accrued equal to the liability for the IBNR employee claims if as of the date of the financial statements there is a legal or contractual requirement for the employer to fund this amount.
- *Employee deferral and related matching contributions for defined contribution plans.* It would be rare that this amount would be significant and therefore this issue will not be included in the EBP Guide.
- *Accounting for excess employee contributions.* Excess employee contributions should be recorded as a liability in the year in which they were contributed to the plan (in accordance with paragraph 3.28 of the EBP Guide) with the corresponding debit side of the entry being netted against contributions received. Additionally, disclosure thereof should be presented in the notes to the financial statements.
- *Presentation of investment income from commingled investment funds.* The EBP Guide should express two views: one that dividends and distributions should be considered investment income and shown separately from changes in fair value, the second that only dividends should be considered investment income and shown separately from changes in fair value.
- *Disclosures for limited partnerships and similar investments.* Additional disclosures should be made relating to limited partnerships and similar investments. The Guide should clarify that these disclosures apply to certain kinds of investments that are hard to value or not liquid (alternative investments). If the information for the disclosures cannot be obtained or is prohibited from being disclosed, then that should be disclosed as well. AcSEC also recommended that the task force look to the disclosures required by the FASB's fair value project.

***Current developments and plans.*** AcSEC will continue its discussions of issues at a future meeting.

Staff: Linda Delahanty

## **Investment Companies Guide—Real Estate Funds**

***Description and background.*** In connection with the anticipated issuance of the SOP *Clarification of the Scope of the Investment Companies Guide* (Scope SOP), parties representing the institutional real estate investment industry approached the AICPA to request a project that would clarify the accounting for private real estate equity funds that are ultimately required by the Scope SOP to follow the Audit and Accounting Guide *Investment Companies* (IC Guide). At present, it is generally acknowledged that the guidance in the IC Guide is insufficient to enable consistent accounting practices among real estate funds applying the IC Guide. Accordingly, AcSEC decided to develop an additional, nonauthoritative chapter of the IC Guide on real estate funds. AcSEC subsequently decided to issue guidance in the form of nonauthoritative questions and answers (Q&As) rather than in the form of a nonauthoritative chapter of the IC Guide.

The project is expected to provide guidance on, among other things—

- The definition of a real estate investment.
- Balance sheet presentation of investments, including the applicability of a consolidation approach to the financial statement presentation.
- Income statement presentation of net investment income, including the applicability of recognizing rental revenue, expenses, or other "accrual" basis earnings in net investment income (versus the dividend income principle noted in the IC Guide).
- Accounting for third-party real estate financing.
- Other financial statement presentation and disclosure matters.

The project will not change existing GAAP, for example, contained in the IC Guide; it will only provide guidance on applying existing GAAP to real estate funds.

***Tentative conclusions.*** At its May 2006 meeting, AcSEC tentatively concluded that—

- The determination of whether a distribution received by an investment company is a return of capital should be based on tax basis earnings and profits.
- If an investment company holds a fee simple interest in a real estate investment, distributions representing income from that investment should be presented as a single income statement line item.

At the September 2007 meeting, AcSEC discussed a series of proposed Q&As and tentatively agreed that—

- For fee-simple interests in real estate, the Guide mandates displaying investment income as a single line item (thereby prohibiting the display of rental income, rental expenses, and so forth).

- The Guide requires that net cash flow received from a fee-simple interest in real estate be allocated between investment income and return of capital based on a notion of economic earnings, such as GAAP-basis earnings (which considers depreciation and amortization) or tax-basis earnings and profits.
- For fee-simple interests in real estate, the net cash flow received by the investment company need not be allocated between investment income and return of investment based on tax-basis earnings and profits.
- AcSEC will express a preference for basing the allocation on tax-basis earnings and profits.

Some AcSEC members did not have the benefit of educational sessions on this topic that were held before those members joined AcSEC, however, and AcSEC agreed to revisit these conclusions at the November 2007 AcSEC meeting. Task force representatives agreed to lead an educational session for new AcSEC members prior to the November 2007 AcSEC meeting.

At the November 2007 AcSEC meeting, AcSEC agreed that—

- For fee-simple interests in real estate, the Guide mandates displaying investment income as a single line item (thereby prohibiting the display of rental income, rental expenses, and so forth).
- The Guide requires that net cash flow received from a fee-simple interest in real estate be allocated between investment income and return of capital based on a notion of economic earnings, such as GAAP-basis earnings (which considers depreciation and amortization) or tax-basis earnings and profits.
- For fee-simple interests in real estate, the net cash flow received by the investment company need not be allocated between investment income and return of investment based on tax-basis earnings and profits.
- AcSEC will express a preference for basing the allocation on tax-basis earnings and profits.

AcSEC asked the task force to revise the Q&As to reflect those votes, and in doing so, to—

- Define “economic earnings” early in the document. The definition should state that economic earnings includes depreciation using reasonable useful lives and should describe the boundaries of what may be considered a measure of economic earnings.

- State in the Q&As that whether a reporting entity uses tax-basis earnings and profits, GAAP-basis earnings, or something else as its measure of economic earnings is an accounting policy decision.

AcSEC reviewed the first 30 Q&As and made a number of recommendations to clarify, improve, and make them consistent with the votes taken.

***Current developments and plans.*** At its January 2008 meeting, AcSEC continued the discussion from its November meeting of a series of proposed questions and answers (Q&As) addressing implementation matters that affect real estate funds that are considered investment companies.

AcSEC agreed that, if the FASB places an indefinite deferral on the effective date of SOP 07-1, *Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies* (which the FASB subsequently did), a recommendation will be made that the provisions of EITF Topic D-74 that limit which entities are or are not subject to the investment companies Guide should be modified to allow entities more latitude in determining whether they are subject to the Guide.

AcSEC discussed those Q&As it had not discussed previously as well as those Q&As that the task force had modified in response to comments from previous AcSEC discussions. AcSEC made a number of recommendations to clarify and improve the Q&As. In addition, AcSEC recommended the elimination of Q&As no. 2, 37, and 38. AcSEC expects to continue discussion of this topic at a future meeting.

Staff: Fred Gill

## **Entities With Oil and Gas Producing Activities**

***Description and Background.*** The AICPA Audit and Accounting Guide *Audits of Entities With Oil and Gas Producing Activities* (the Oil and Gas Guide) was originally issued in 1986. The Oil and Gas Guide has not been revised or amended, other than for conforming changes, since its issuance.

Substantial industry changes have resulted in the emergence of many new accounting and auditing issues, as well as the need to revise the industry background section of the Oil and Gas Guide. In addition, new standards have been issued and other issues that have a direct effect on the accounting for oil and gas operations have been raised by regulators. Many of the accounting issues have led to diversity in practice.

In 2004, a task force began work on a project to revise the Oil and Gas Guide.

***Tentative conclusions.*** Some of the tentative conclusions reached by AcSEC in discussing the Oil and Gas Guide are as follows:

- *May a nonpublic entity apply the full cost method in any manner other than as prescribed by the SEC (i.e., as prescribed in Regulation S-X, Rule 4-10)? In particular, must nonpublic entities apply such guidance related to the designation of cost centers?* AcSEC believes that it is preferable that nonpublic entities that apply the full cost method of accounting follow the guidance prescribed by the SEC in Rule 4-10 of Regulation S-X. Furthermore, AcSEC would like to make a broader statement regarding preferability, stating that AcSEC believes that nonpublic entities should follow the guidance in either FASB Statement No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies*, for successful efforts entities or the SEC full cost rules, as guidance for these methods is periodically updated. Additionally, AcSEC would like the Guide to mention that the entity may apply FASB Statement No. 154, *Accounting Changes and Error Corrections*, to make the change to a preferable accounting method.
- *For entities using the full cost method of accounting, should gains or losses resulting from the settlement of asset retirement obligations be reflected in income or capitalized through application of Regulation S-X, Rule 4-10?* At a minimum, AcSEC would like the Guide to lay out the issue and provide some guidance based on what is done in practice but declined to express a preference. Based on the observations of the task force, most entities reflect gains or losses resulting from AROs as an adjustment of capitalized costs.
- *Can any sale of a property included in the amortization base qualify for reporting as a discontinued operation by an entity applying the full cost method of accounting?* When applying FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, an entity following the full cost method would determine that a component under Statement No. 144 would be an individual full cost pool. Therefore, an entity would not meet the criteria for reporting a discontinued operation unless an entire pool was disposed of. AcSEC recommended that the Guide reflect this observation.
- *For entities using the full cost method, may costs incurred in a new cost center prior to the acquisition of a property interest or prior to determination of proved reserves remain capitalized in situations in which the company has plans for acquisition of property interests or further exploration activity?* AcSEC supported the Oil and Gas Task Force's view that the application of the full cost ceiling test should be deferred/suspended in certain circumstances associated with consideration/execution of an exploration plan in a new country.

***Current developments and plans.*** In November 2007, AcSEC had an initial discussion of three chapters of a proposed revised Oil and Gas Guide:

- Chapter 2, Successful Efforts Method of Accounting for Oil and Gas Activities
- Chapter 3, Full Cost Method of Accounting for Oil and Gas Activities
- Chapter 4, Accounting for International Oil and Gas Activities

AcSEC made a number of recommendations to clarify and improve the draft chapters.

In May 2008, AcSEC reviewed the changes made in response to its November 2007 discussion of chapters 2, 3, and 4 of the proposed Guide and also had an initial discussion of two other chapters of the proposed Guide:

- Chapter 1, Overview of the Industry
- Chapter 5, Accounting for International Oil and Gas Activities

AcSEC made a number of recommendations to further clarify and improve the draft chapters, among them moving guidance on accounting for common oil and gas ownership arrangements into a freestanding chapter.

AcSEC expects to continue its discussion at a future meeting with a view toward approving issuance of the proposed Guide for public comment.

Staff: Fred Gill

## **Not-for-Profit Organizations Audit and Accounting Guide**

***Description and background.*** The AICPA Audit and Accounting Guide *Not-for-Profit Organizations* (NPO Guide) was originally issued in 1996. The NPO Guide has not been revised or amended, other than for conforming changes, since its issuance. Various issues have arisen since the issuance of the Guide including but not limited to issues not contemplated in the existing Guide, issues arising as a result of the conforming change process, and issues arising in implementing the Guide. Some of the accounting issues have led to diversity in practice.

In 2005, a task force began work on a project to revise the NPO Guide.

***Tentative conclusions.*** Some of the tentative conclusions reached by AcSEC in discussing the NPO Guide are as follows:

- *Special events that will be held after year-end, for which amounts are received before year-end.* The ticket price of a special event that will be held after year-end, for which amounts are received before year-end, should be bifurcated between the portion pertaining to the cost of the event (exchange transaction) and the portion pertaining to the contribution element. The portion of the amount received in advance of the event pertaining to the contribution is presumed to be conditioned on the event taking place.

Accordingly, it should be accounted for in conformity with paragraph 22 of FASB Statement No. 116, *Accounting for Contributions Received and Contributions Made*, and considered a refundable advance. The exchange transaction portion should be recognized when earned (that is, when the event takes place), in conformity with the same principles that govern recognition of revenue from other kinds of exchange transactions.

- *Accounting for contributions of certain nonfinancial assets, such as fund-raising or informational material or advertising, including media time or space for public service announcements or other purposes.* Nonfinancial assets, such as fundraising material, informational material, or advertising, including media time or space for public service announcements or other purposes that are used for the NPO's benefit (or provided to the NPO at no charge) and that encourage the public to contribute to an NPO or help the NPO communicate its message or mission should be reported as contributions when received. The NPO has not received the asset (and has, therefore, not received a contribution) in circumstances in which the NPO is unable to have active involvement in determining and managing the message and the use of the materials. In determining fair value [the price that would be received to sell the media time or space in an orderly transaction between market participants at the measurement date], entities should consider all facts and circumstances.
- *Net asset classification - correction of an error.* In considering whether an item is a correction of an error, individual net asset classes, rather than net assets in aggregate, are relevant in determining whether an item is a correction of an error.
- *Performance indicator/measure of operations.* A particular entity's definition of *operations* is an accounting policy that should be applied consistently and disclosed; *operations* may have a different meaning in the statement of cash flows than it does on the statement of activities.
- *Should subsequent events be considered in determining whether conditions are met or remote?* Recognition and measurement should be based on facts and circumstances existing at the reporting date. A subsequent change in facts and circumstances should be recognized in the period in which the change occurs. Accordingly, a change in facts subsequent to the reporting date but prior to the issuance of the financial statements should be recognized in the period in which the change in facts occurs. Subsequent events that provide information about facts and circumstances that existed at the date of the financial statements should be considered in determining whether the conditions are substantially met at the date of the financial statements.

Paragraph 22 of FASB Statement No. 116 provides that "a conditional promise to give is considered unconditional if the possibility that the condition will not be met is remote." The task force will clarify in the Guide that that determination is made on day one, and not subsequently.

- *Naming opportunities and similar forms of public recognition.* Although in some cases public recognition (and other rights and privileges) does not result in significant value to the resource provider, and therefore should be reported as contributions, NPOs should consider whether such transactions are in fact contributions, exchange transactions, or some combination of both. In circumstances in which the transaction is bifurcated between a contribution and an exchange transaction, AcSEC believes organizations should first determine the fair value of the exchange transaction, with the residual reported as contributions.
- *Promise to give to be funded after a donor's death.* Assuming that the promise is made by the donor and is not merely naming the NPO in a will that could be changed, the donor has made an unconditional contribution. As such, NPOs should report the promise to give as a contribution, measured at its fair value. The ability of a donor to deplete assets does not constitute a condition under FASB Statement No. 116 that would preclude recognition of a contribution. Fair value should be measured pursuant to FASB Statement No. 157, *Fair Value Measurements*. In measuring the fair value of the contribution, the NPO should consider the terms of the contribution and other inputs, such as the donor's mortality; whether sufficient assets will exist to fulfill the promise; and the anticipated date of distribution of assets to the NPO. Consideration and assessment of the inputs requires judgment and may lead to a low estimate of fair value (including zero), depending in particular on the funding for the promise and expected date of death.
- *Endowment funds - ambiguous donor stipulations that create uncertainty about net assets classifications.* Donor intent is the overriding factor in determining net asset classifications. All other facts and circumstances are information to help determine donor intent. In fact patterns in which donor stipulations are ambiguous but could reasonably be interpreted to intend that the contribution is permanently restricted, a presumption exists that the net asset classification should be permanently restricted unless clear direction from the donor to the contrary exists.
- *Reporting investment expenses.* The NPO Guide should be revised to clarify that *investment expenses* include costs of activities conducted by the NPO or directly on its behalf to generate an investment return. It would be desirable if the FASB revised FASB Statement No. 117 to (a) eliminate the requirement in paragraph 24 that the amount of investment expenses be disclosed in circumstances in which investment revenues are reported net of related expenses and (b) require that total return be reported net of investment expenses. At a future date, AcSEC will consider whether it wishes to formally request the FASB to make such a revision.
- *Error in 2000 conforming change process —SFAS 136 trustee reporting--Chapter 6 FN 1.* As part of the 2008 conforming changes, footnote 1 to Chapter 6 of the NPO

Guide should be deleted and no guidance on trustee accounting in this circumstance should be provided. In addition, the task force should explain in the Guide the reason for deleting the footnote and providing no guidance, as well as the fact that the guidance in the deleted footnote was not inconsistent with FASB Statement No. 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others*. The NPO Guide task force should reconsider this issue (for the ongoing guide project) and present its conclusions to AcSEC at a future meeting. The task force should reframe the issue, considering factors and issues such as (1) distinctions between holding the assets as trustee versus not as trustee, (2) distinctions between being the direct beneficiary versus being financially interrelated to the direct beneficiary, (3) basis for grossing up the assets and liabilities (a consolidation model), rather than reporting merely the NPO's beneficial interest, (4) task force conclusions in relation to the guidance currently in the Guide (which guidance the task force proposes retaining and which guidance the task force proposes revising), (5) other potentially analogous authoritative literature, such as SOP 94-3, *Reporting on Related Entities by Not-for-Profit Organizations*, and EITF Issue 90-15, "Impact of Nonsubstantive Lessors, Residual Value Guarantees, and Other Provisions in Leasing Transactions," and (6) what happens if the trustee goes into bankruptcy.

- *Incorporate existing NPO TPAs Into the NPO Guide*

Incorporate the conclusions of the following TPAs in the guide, subject to any comments as noted below:

- 6140.01 *Inventory Valuation for a Not-for-Profit Scientific Organization* - While AcSEC does not object to the conclusion in this TPA, revisit with the NPO EP/TF whether it is necessary to include it in the Guide.

- 6140.02 *Income Recognition of Membership Dues by Not-for-Profit Organization*

- 6140.03 *Lapsing of Time Restrictions on Receivables That Are Uncollected at Their Due Date*

- 6140.04 *Lapsing of Restrictions on Receivables if Purpose Restrictions Pertaining to Long-Lived Assets Are Met Before the Receivables Are Due*

- 6140.05 *NPO Accounting for Loans of Cash That Are Interest Free or That Have Below-Market Interest Rates* - Clarify that the conclusions in this TPA do not apply to transactions between parents and subsidiaries; remind readers to consider the disclosure requirements of FASB Statement No. 57, *Related Party Transactions*; revise the method for determining fair value to be flexible, consistent with the model in FASB Statement 157, *Fair Value Measurements*.

- 6140.06 *Functional Category of Cost of Sales of Contributed Inventory*

- 6140.07 *Functional Category of Costs of Special Events*
- 6140.08 *Functional Category of the Costs of Direct Donor Benefits*
- 6140.09 *Reporting Bad Debt Losses*
- 6140.10 *Consolidation of Political Action Committee* - Consider the implications of EITF Issue 90-15, *Impact of Nonsubstantive Lessors, Residual Value Guarantees, and Other Provisions in Leasing Transactions* and 96-21, *Implementation Issues in Accounting for Leasing Transactions Involving Special-Purpose Entities*. In that regard, consider whether a political action committee typically is an NPO, for-profit entity, or SPE for purposes of applying GAAP.
- 6140.11 *Costs of Soliciting Contributed Services and Time That Do Not Meet The Recognition Criteria in FASB Statement No. 116*
- 6140.12 *Nondiscretionary Assistance Programs*
- 6140.14 *Application of FASB Statement No. 136—Classification of a Beneficiary’s Interest in the Net Assets of a Financially Interrelated Fund-Raising Foundation* (The beneficiary can influence the operating and financial decisions of the foundation to such an extent that the beneficiary can determine the timing and amount of distributions from the foundation.)
- 6140.15 *Application of FASB Statement No. 136—Classification of a Beneficiary’s Interest in the Net Assets of a Financially Interrelated Fund-Raising Foundation* (The beneficiary cannot influence the operating and financial decisions of the foundation to such an extent that the beneficiary can determine the timing and amount of distributions from the foundation.)
- 6140.16 *Application of FASB Statement No. 136—Classification of a Beneficiary’s Interest in the Net Assets of a Financially Interrelated Fund-Raising Foundation* (More Than One Beneficiary—Some Contributions Are Designated)
- 6140.17 *Application of FASB Statement No. 136—Classification of a Beneficiary’s Interest in the Net Assets of a Financially Interrelated Fund-Raising Foundation* (The beneficiary makes an expenditure that meets a purpose restriction on net assets held for its benefit by the recipient organization—The beneficiary can influence the operating and financial decisions of the recipient to such an extent that the beneficiary can determine the timing and amount of distributions from the recipient.)
- 6140.18 *Application of FASB Statement No. 136—Classification of a Beneficiary’s Interest in the Net Assets of a Financially Interrelated Fund-Raising Foundation* (The beneficiary makes an expenditure that is consistent with a purpose restriction on net assets held for its benefit by the recipient organization—

The beneficiary cannot influence the operating and financial decisions of the recipient to such an extent that the beneficiary can determine the timing and amount of distributions from the recipient.)

- 6140.20 *NPOs Reporting No Fund-Raising Expenses*
- 6140.21 *Should an NPO Report Amounts Charged to the NPO by a Professional Fund-Raiser Gross, as Fund-Raising Expenses, or Net, as a Reduction of Contributions?*
- 6140.22 *In Circumstances in Which the Reporting NPO Undertakes a Transaction in Which Another NPO (Fund-Raising NPO) Raises Contributions on Behalf of the Reporting NPO, and the Reporting NPO Compensates the Fund-Raising NPO for Raising Those Contributions (Compensation Including, But Not Limited to, an Administrative Fee), Should the Reporting NPO Report the Fund-Raising NPO's Compensation Gross, as Fund-Raising Expenses, or Net, as a Reduction of Contributions?*
- *Remainder Interests in Noncash Assets* – The NPO Guide should address this issue. AcSEC supports a gross presentation, with a credit to reflect a lease. In applying FASB Statement No 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, consider the carrying amount of the asset to be the gross amount less any related deferrals or liabilities. The Task Force should revisit the day 2 accounting, including, but not limited to, the character and name of the balance sheet credit, whether the asset should be considered an investment or rental property, whether the asset should be depreciated and/or reported at fair value, and whether the liability should be adjusted in subsequent periods.
- *Voluntary Health and Welfare Organizations and the Statement of Functional Expenses* - AcSEC believes the criteria for requiring a SFE as a basic statement should be as follows:
  - Not-for profit organizations should be required to present a statement of functional expenses as a basic financial statement if they are supported by the general public. A not-for-profit organization is presumed to be supported by the general public if contributions are significant to total revenue and support, including both cash and in-kind contributions recognized in the financial statements, but excluding government support.
  - In limited cases, an organization may receive significant amount of contributions but be able to rebut the presumption that it is supported by the general public. (Thus, it would not be required to present a statement of functional expenses.) Examples of evidence that rebuts the presumption that an organization is supported by the general public include:

- Contributions are solely from a single donor, such as an individual or a single private foundation (or a limited number of donors), whose reporting requirements are met through other means.
  - A large, nonrecurring contribution from a single donor caused the NPO to meet the “significant portion” threshold in the current year.
  - Contributions are solely from donors that clearly are not representative of the general public because their reporting requirements are met through other means (such as contributions solely from members of the governing board).
- If an organization is required to present a statement of functional expenses in a given year, it should continue to present that statement annually unless there is a change in the nature of the primary support that management expects to be of a continuing nature. An organization shall determine whether there has been a change in the nature of the primary support at least annually, or more often if the facts and circumstances indicate that there has been a change in the nature of a reporting unit’s primary support. Annual evaluations may be performed any time during the year if the evaluation is performed at the same time every year. The results of the evaluation would then impact whether a statement of functional expenses is presented as a basic statement for the next subsequent set of financial statements. Financial statements for a period of change would then be required to include footnote disclosure of the change in kinds of basic financial statements presented.
- A set of financial statements would be considered comparative even if a statement of functional expenses were not presented in each year if the reason for the absence of a year’s statement of functional expenses is that the organization did not meet the criterion requiring presentation for that year. Entities that are not required to present a statement of functional expenses as a basic statement may choose to include similar information as a table in the accompanying footnotes; a schedule of functional expenses presented as supplemental information; or as a basic statement.
  - AcSEC believes that when performing the percentage threshold test of contributions it is sound to continue the NPO Guide precedent of excluding support from governmental entities (just as support from governmental entities were excluded from the definition of public support for determining which organization were VHWOs) because governmental entities have the ability to impose (and practice says they do impose) their own reporting requirements on the NPO to monitor how the governmental resources were used.

- It would be desirable if the FASB revises FASB Statement No. 117, *Financial Statements of Not-for-Profit Organizations*, to reflect the conclusions in the document. At a future date, AcSEC will consider whether it wishes to formally request the FASB to make such revisions.
- *Statement of Functional Expenses - Reporting Major Classes of Programs* - The NPO Guide should more explicitly provide that AcSEC believes NPOs should report the functional expenses of the various programs they conduct; and that providing a single program expense category would be insufficient in most cases. NPOs that have a single program, however, should report using a single program expense category. AcSEC agreed that the NPO Guide should be revised to reflect both of these situations (multiple programs as well as a single program), as well as provide examples of appropriate reporting.
- *Display of Contributions Made* - As part of their program services, some NPOs make contributions to other NPOs, including but not limited to affiliated NPOs. Issues exist about how contributions to others, including grants that are contributions, should be displayed. AcSEC recommends that such contributions to other NPOs be displayed separately from other types of expenses, either in the statement of activities or notes to the financial statements. Contributions to other NPOs, including grants that are contributions, are different in concept from expenses incurred in running an organization's own activities, and that distinction may be meaningful to financial statement users. In addition, AcSEC recommends that payments or other support to affiliates that cannot be allocated to functions and therefore are treated as a separate supporting service pursuant to paragraph 13.57 of the NPO Guide (and reported on a statement of activities as a separate line item and labeled "unallocated payments to affiliated organizations.") be clearly categorized on the statement of activities as *expenses*.
- *Interests in other entities* – AcSEC supports the following overall approach:
  - First determine whether GAAP requires consolidation.
  - If consolidation is not required, then determine whether GAAP requires the equity method of reporting.
  - If neither consolidation nor the equity method is appropriate, then determine whether GAAP requires or permits fair value or cost.

Guidance for determining whether NPOs should consolidate an interest in a for-profit corporation should be the same as guidance for determining whether for-profits should consolidate an interest in a for-profit corporation, except in circumstances in which authoritative GAAP includes scope exceptions pertaining

to NPOs. Identified scope exceptions include (1) NPOs are explicitly scoped out of FIN 46R, *Consolidation of Variable Interest Entities*, except for certain limited exceptions, and (2) certain EITF consensus conclusions (such as 90-15 and 96-21) remain effective for entities other than those within the scope of FIN 46 (R) and therefore apply to NPOs. (This guidance can be included in the guide as the application of existing GAAP.)

Guidance for determining whether NPOs should consolidate an interest in an unincorporated for-profit entity should be the same as guidance for determining whether for-profits should consolidate an interest in an unincorporated for-profit entity, except in circumstances in which authoritative GAAP includes scope exceptions pertaining to NPOs (no such exceptions identified at this time). Along those lines, paragraph 3 of EITF Issue 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights*, should be read as excluding from the scope of EITF Issue 04-5 limited partnership interests that are *required* to be reported at fair value pursuant to GAAP (such as investments in limited partnerships held by investment companies), rather than limited partnership interests that are *permitted* to be reported at fair value pursuant to GAAP (such as investments in limited partnerships reported at fair value pursuant to Appendix A of chapter 8 of the NPO Guide). Given that practice, however, is to exclude from the scope of the EITF Issue 04-5 limited partnership interests that are reported at fair value pursuant to Appendix A of chapter 8 of the NPO Guide, AcSEC should ask FASB to eliminate, through a change to authoritative GAAP, SOP 94-3's provision that reporting investments at fair value in conformity with Appendix A of chapter 8 of the NPO Guide qualifies for the fair value scope exclusion included in EITF Issue 04-5.

Guidance for determining whether NPOs should consolidate an interest in an NPO corporation should be pursuant to SOP 94-3, *Reporting of Related Entities by Not-for-Profit Organizations*.

Guidance for determining whether NPOs should consolidate an interest in an unincorporated NPO entity should be pursuant to paragraph 10 of SOP 94-3. NPOs should look to the partnership agreement or other analogous document to determine whether the NPO has a controlling financial interest through direct or indirect ownership of a majority voting interest in that unincorporated entity. NPOs should consider EITF and other authoritative literature in making this determination. It would be irrelevant whether the entity in which the NPO has an interest is mission related, or whether the interest is in real estate.

In determining whether the equity method of accounting is appropriate for an interest in an NPO:

- No distinction should be made between interests in entities that are mission related versus not mission-related.
- No distinction should be made between interests in corporations vs. interests in unincorporated entities.
- As an overall model, consider whether the reporting NPO has ability to exercise significant influence and an ownership interest. The existence of both leads to the equity method.
- Consider the guidance in APB 18 and related guidance (including EITF Topic D-46, *Accounting for Limited Partnership Interests*), pertaining to determining whether the NPO has ability to exercise significant influence.
- Consider the guidance in the EITF Issue 02-14, *Whether an Investor Should Apply the Equity Method of Accounting to Investments Other than Common Stock*, including whether the NPO has risks and rewards of ownership.
- An ownership interest exists if (1) the reporting entity has a right to or a responsibility for the operating results of another entity, or (2) upon dissolution of another entity, the reporting entity is entitled to the net assets, or is responsible for any deficit, of that other entity. (These conditions are taken from the definition of an *economic interest* in Chapter 3 of the NPO guide.)

In circumstances in which an ownership interest exists, reporting alternatives include potentially the equity method (if coupled with ability to exercise significant influence), fair value (if the NPO has an ownership interest but not ability to exercise significant influence -- FAS 159 and App A to chapter 8), or cost (if the NPO has an ownership interest but not ability to exercise significant influence).

In circumstances in which an NPO transfers resources to another entity, and the equity method is not the appropriate accounting, the debit would be to either contribution expense, loan receivable, or some other type of asset represented by contractual rights (rather than an ownership interest).

AcSEC directed the task force to consider these conclusions, revise the document as appropriate, identify additional issues to be resolved, and bring the document back to AcSEC.

At May 2008 meeting, AcSEC discussed the following issues summaries and had the following comments:

Reporting Unconditional promises to give the use of long-lived asset—not to exceed FV  
The guide should be revised to provide that amounts reported as contributions of the use of long-lived assets at the date the unconditional promise to give is received (and the contribution recognized) should not exceed the fair value of the underlying long-lived asset at that date. AcSEC observed that inherent in that conclusion is the notion that in some circumstances, the NPO may receive contributions in addition to the use of the long-lived asset, such as promises to pay executory costs, make renovations, or address environmental remediation obligations.

#### Contributed Use of Facilities - Journal Entries

The donor should credit rent income. Consider the guidance in FASB Statement of Concepts No. 6, *Elements of Financial Statements*, particularly paragraphs 78, 79, and 82, in determining the classification of that income as revenue or other income on the statement of activities.

The task force should consider whether it wishes to continue pursuing guidance about the journal entries. If the task force does wish to continue pursuing guidance about the journal entries, it should consider:

- What did the NPO receive? For example, an intangible asset or the equivalent of a prepaid lease?

- Is it appropriate to accrete the discount on a promise to give a nonmonetary asset (and generate additional revenue)? What if that nonmonetary asset is an intangible asset?

#### Treatment of HUD Advances and Related Interest

AcSEC agreed (8 yes) that the task force should develop a framework for further analysis of the issue. (6 AcSEC members supported the task force conclusion, revised to reflect an interest accrual in circumstances in which a loan is reported.) In particular, the task force should:

- Review and document various types of prevalent agreements and fact patterns.
- With an aim toward developing prescriptive guidance, consider which attributes of those agreements and fact patterns would lead to the various conclusions (loan, contribution, or exchange transaction)

In circumstances in which a loan is reported, the NPO also should accrue interest. Several AcSEC members expressed a leaning toward reporting exchange transactions, and an aversion to reporting a contribution on day one. Of those expressing a leaning toward reporting exchange transactions, some observed that the revenue recognition model could be to recognize revenue either (a) systematically and ratably over the life of the agreement or (b) at the end of the agreement. AcSEC directed the task force to consider other GAAP addressing revenue recognition, and suggested that support could be found by analogy for both models (a) and (b) in the previous sentence.

***Current developments and plans.*** AcSEC will continue its discussions at future meetings.

Staff: Joel Tanenbaum

## **Property and Liability Insurance Companies Audit and Accounting Guide**

***Description and background.*** The AICPA Audit and Accounting Guide *Property and Liability Insurance Companies* was last issued in 1990. The Guide has not been revised or amended, other than for conforming changes, since its issuance. Various issues have arisen since the issuance of the Guide, including but not limited to issues not contemplated in the existing Guide due to the evolving insurance environment and issues arising as a result of the conforming change process.

In 2006, a task force began work on a project to revise the property and liability insurance Guide.

***Current developments and plans.*** At its March 2008 meeting, AcSEC discussed a revised draft of chapter 4, “The Loss Reserving and Claims Cycle,” of a proposed revised Audit and Accounting Guide *Audits of Property and Liability Insurance Companies*. AcSEC suggested a number of clarifications to chapter 4.

AcSEC also tentatively concluded the following in discussing the Property & Liability Insurance Guide:

- *Disclosure of interest and dividend income for investments under FASB Statement No. 115.* The Guide will include discussion of current practice of where on the statement of income insurance companies generally include interest and dividend income related to available-for-sale securities and trading securities. The Guide will also include a recommendation that insurance companies disclose where interest and dividend components are included in the statement of income.

At a future AcSEC meeting, the Property and Liability Insurance Guide Task Force will discuss the Premium Chapter and revisit some open items in the Loss Reserves Chapter.

Staff: Kim Kushmerick

## NON-AcSEC ACTIVITIES OF AICPA STAFF

The AICPA Investment Companies Expert Panel and staff issued four **investment companies-related Technical Practice Aids (TPAs)** to provide guidance on the following topics.

- TPA 6910.25, *Considerations in Evaluating Whether Certain Liabilities Constitute "Debt" for Purposes of Assessing Whether an Investment Company Must Present a Statement of Cash Flows*
- TPA 6910.26, *Additional Guidance on Determinants of Net vs. Gross Presentation of Security Purchases and Sales/Maturities in the Statement of Cash Flows of a Nonregistered Investment Company*
- TPA 6910.27 *Treatment of Deferred Fees*
- TPA 6910.28, *Reporting Financial Highlights, Net Asset Value (NAV) Per Share, Shares Outstanding, and Share Transactions When Investors In Unitized Non-registered Funds Are Issued Individual Classes or Series of Shares*

The TPAs are available on the AICPA's website at

[http://www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+Standards/recent\\_tpas.htm](http://www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+Standards/recent_tpas.htm)

### **AICPA Publishes Article on Tax-Exempt debt—Geared toward entities issuing the debt.**

The AICPA has posted to its website a nonauthoritative article authored by an ad hoc group of AICPA members, *Tax-Exempt Bonds - Accounting and Auditing Considerations in the Current Environment*. The article has a particular focus on debt that is referred to as (1) auction rate securities (ARSs) and (2) variable rate demand obligations (VRDOs), and provides issuers of tax-exempt debt and their auditors an overview of the accounting and auditing considerations that may be relevant in light of recent market events and entity transactions. While the current environment presents accounting and auditing issues for investors in that tax-exempt debt, the article focuses on issues facing the issuers of that debt.

The article can be accessed at

[http://www.aicpa.org/download/acctstd/ARS\\_article14.pdf](http://www.aicpa.org/download/acctstd/ARS_article14.pdf)

## UPCOMING AcSEC MEETINGS

AcSEC meetings are open to the public.

### 2008

July 15-16, 2008	Chicago, IL
September 23-24, 2008	NY
November 18-19, 2008	TBD

### 2009

January 13-14, 2009	New York
March 24-25, 2009	New York
May 19-20, 2009	New York
July 14-15, 2009	TBD
September 22-23, 2009	New York
November 17-18, 2009	TBD

## AcSEC ON AICPA WEB SITE

Visit the Accounting Standards webpage, located on the AICPA website, at <http://www.aicpa.org/members/div/acctstd/index.htm>, to view information about AcSEC activities, including AcSEC's meeting agenda and materials, highlights of recent AcSEC meetings, and to obtain a copy of recently issued AcSEC's documents, learn about the AICPA Industry Expert Panels, review recently issued accounting technical practice aids, and find web links to accounting standard setting bodies, regulators, and other AICPA technical teams.

### **AICPA's Business Reporting Assurance & Advisory Services (BRAAS) team**

The overarching role of the [AICPA's Business Reporting Assurance & Advisory Services \(BRAAS\) team](#) is to provide oversight, direction, project management, and visioning for emerging business reporting and assurance issues and initiatives that are identified and developed through input from AICPA members, committees, and staff. The BRAAS Team is currently working on three major initiatives that support the Team's goals related to business reporting and assurance: XBRL, Enhanced Business Reporting, and various Assurance Services Executive Committee projects. To learn more about these initiatives, visit <http://www.aicpa.org/Professional+Resources/Accounting+and+Auditing/BRAAS/>

## COMMENTS OR SUGGESTIONS?

We welcome any comments or suggestions you may have concerning this publication. Please send them to [iportnoy@aicpa.org](mailto:iportnoy@aicpa.org), fax to 212-596-6064, or write to Irina Portnoy at AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775.

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The views expressed herein are those of the authors and do not necessarily reflect the views of the American Institute of Certified Public Accountants. Official positions of the AICPA are determined through specific committee procedures, due process, and deliberations.

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