

**SELF-STUDY CONTINUING PROFESSIONAL EDUCATION**

# **Decoding the FASB Codification**

Fort Worth, Texas  
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#### Registration Numbers

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## INTRODUCTION

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### Taking the Course

You are asked to read the material and, during the course, to test your comprehension of each of the learning objectives by answering self-study quiz questions. After completing each quiz, you can evaluate your progress by comparing your answers to both the correct and incorrect answers and the reason for each. References are also cited so you can go back to the text where the topic is discussed in detail. Once you are satisfied you understand the material, **answer the examination questions which follow each lesson and record your answer choices by logging on to our Online Grading System.**

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CPE requirements are established by each state. You should check with your state board of accountancy to determine the acceptability of this course. We have been informed by the North Carolina State Board of Certified Public Accountant Examiners and the Mississippi State Board of Public Accountancy that they will not allow credit for courses included in books or periodicals.

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## Decoding the FASB Codification (CODTG10)

### OVERVIEW

<b>COURSE DESCRIPTION:</b>	This interactive self-study course covers the basic aspects of the FASB Accounting Standards Codification™ (ASC), including a historical perspective, implementation date, how ASC interfaces with XBRL and IFRS, and the mechanics of ASC.
<b>PUBLICATION/REVISION DATE:</b>	August 2010
<b>PREREQUISITE/ADVANCE PREPARATION:</b>	Basic knowledge of GAAP
<b>CPE CREDIT:</b>	4 QAS Hours, 4 Registry Hours  Check with the state board of accountancy in the state in which you are licensed to determine if they participate in the QAS program and allow QAS CPE credit hours. This course is based on one CPE credit for each 50 minutes of study time in accordance with standards issued by NASBA. Note that some states require 100-minute contact hours for self-study. You may also visit the NASBA website at <a href="http://www.nasba.org">www.nasba.org</a> for a listing of states that accept QAS hours.
<b>FIELD OF STUDY:</b>	Accounting
<b>EXPIRATION DATE:</b>	<b>August 31, 2011</b>
<b>KNOWLEDGE LEVEL:</b>	Basic

### LEARNING OBJECTIVES

#### Lesson 1: Decoding the FASB Codification

Completion of this lesson will enable you to:

- Explain why the Codification was needed, identify who authorized the project and when, and explain who is affected.
- Identify the different components of the Codification and how it differs from the pre-ASC GAAP hierarchy.

#### Lesson 2: Codification and Convergence

Completion of this lesson will enable you to:

- Identify differences between IFRS and U.S. GAAP.
- Identify ongoing developments as FASB and IASB standards converge under the Memorandum of Understanding (MoU) between the two Boards.

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# Lesson 1: Decoding the FASB Codification

## Learning Objectives

Completion of this lesson will enable you to:

- Explain why the Codification was needed, identify who authorized the project and when, and explain who is affected.
- Identify the different components of the Codification and how it differs from the pre-ASC GAAP hierarchy.

## Introduction

Webster defines codification as “the act, process, or result of arranging in a systematic form or code.” On June 3, 2009, the FASB voted to approve the FASB Accounting Standards Codification™ (ASC); what is known as U.S. GAAP. This codification will forever change the way accounting research is performed. Accountants who prepare financial statements will be affected the most by this change. The Codification brings accounting research into the digital age, but it also prepares U.S. GAAP for conversion to International Financial Reporting Standards (IFRS). Among other things, this course will explore what ASC means to accountants, when it is effective, what it does, and why such a program is needed in the first place. Also discussed is the impact of the Codification on XBRL and the move to adopt IFRS.

## Why Did We Need the Codification?

Over the last ninety years or so the number of authoritative pronouncements issued by the FASB, AICPA, their predecessor organizations and countless other standard-setters have numbered in the thousands. Practitioners had to look for conflicts, amendments, and superseded statements when following authoritative GAAP guidance. In addition, there was not defined organization within each standard to assist practitioners when researching. The 1990's and early 21<sup>st</sup> century saw perhaps some of the most egregious cases of fraud and mismanagement. Companies like Enron, WorldCom, Waste Management, and Computer Associates, were just a few of the companies whose names were smeared by scandal. Many believed that the complex and often difficult to follow accounting standards contributed to these failures.

There was plenty of blame to go around, and some felt that the regulators had failed to provide proper oversight of these companies who used the complexity and sheer volume of accounting standards to camouflage their misdeeds:

- The Securities and Exchange Commission (SEC), International Accounting Standards Committee (IASC), Public Oversight Board (POB), American Institute of Certified Public Accountants (AICPA), Financial Accounting Standards Board (FASB), and others faced scrutiny and criticism on several fronts, not the least of which was FASB's rule concerning Special Purpose Entities (SPE); FASB's continued existence was reportedly in question, although in FASB's defense, changes it proposed during the years that preceded the meltdown were opposed by corporate America, the big accounting firms, and congressional leaders. FASB, in turn, tried to explain its role as an authoritative body and suggested that Congress should be involved in the overall process of FASB oversight without interfering in the process of technical decision-making.

- The POB was disbanded by the SEC and the Sarbanes-Oxley Act of 2002 (SOX) was enacted, thereby creating the Public Company Accounting Oversight Board (PCAOB) to oversee auditors of public companies.
- “Transparency” became a frequently-used word when describing efforts to resolve perceived problems in the system.
- In 2003, certain steps that had already been taken toward international convergence of accounting standards and financial reporting, and on developing a single source of GAAP (excluding SEC guidance); the development of and maintenance for which FASB would be responsible.

The end result was the FASB Accounting Standards Codification™ (ASC) project. By itself, ASC can only do so much to promote international standards convergence—but it is critical to the process of streamlining GAAP standards and designating a sole authoritative source for the U.S. GAAP XBRL taxonomy.

## Overview of the Project

With over 2,000 pronouncements accumulated over a 70-year period, and estimated to fill the equivalent of 20,000 pages, U.S. GAAP had become badly bloated, overly complex, and almost impossible to navigate. In the words of FASB Chair, Robert Herz, “In technical terms, it’s nuts.”

In September 2004, the Trustees of the Financial Accounting Foundation (FAF), the FASB’s oversight board, approved a 4-year project that involved over 200 people, the cost of which has been estimated at approximately \$16 million, with the following objectives:

- Clarify the authoritative status of accounting literature,
- Reduce the time and effort necessary to research issues,
- Improve the usability of GAAP and mitigate the risk of noncompliance,
- Provide a platform for real-time updating as new standards are released,
- Facilitate a smoother path to convergence with international financial reporting standards, and
- Support the development of the U.S. taxonomy for eXtensible Business Reporting Language (XBRL).

In developing the ASC, the FASB sifted through thousands of pages of nongovernmental accounting pronouncements in order to organize them into the 90 topics of the new GAAP hierarchy.

FASB released the ASC project on January 15, 2008 for a one year verification period. In essence, ASC represents a major restructuring of authoritative guidance for levels A–D of the GAAP hierarchy. The previous four levels of the GAAP hierarchy have been reduced to two levels—authoritative and non-authoritative. This restructuring will affect all non-governmental U.S. entities, and has become the single source of authoritative GAAP for those entities (excluding SEC guidance). While certain SEC guidance is also included in the codification, ASC will not be the source of SEC guidance. ASC also includes some “grandfathered” material, but outdated or nonessential material is not included and neither will guidance for non-GAAP issues such as those concerning other comprehensive basis of accounting (OCBOA). The Codification excludes grandfathered GAAP because it can no longer apply the guidance to new transactions.

## Oversight and Effective Date

In January 2009, FASB officially completed the verification phase of the ASC project. On January 15, 2009, the deadline for feedback, FASB released its codification and related online research system. Originally intended to become effective in April 2009, ASC was delayed until mid-2009.

The Codification became effective on July 1, 2009. At that time, the Codification became the single source of authoritative U.S. GAAP for all nongovernmental entities, superseding all non-SEC accounting and reporting standards. The Codification is the initial step in preparing U.S. accounting standards for convergence with the International Financial Reporting Standards. The FASB will no longer maintain or update the superseded standards.

While the Codification does not intend to modify GAAP, it does introduce a new structure that is organized in an easily accessible online research system. Developers of the new system expect that it will substantially reduce the time and effort needed to research accounting issues. FASB product developers say that there have been no changes in GAAP, however, there is one change. The change incorporated into the Codification the AICPA's TIS 5100, *Revenue Recognition*, paragraphs 38–76, relating to software revenue recognition. (All other TIS are considered nonauthoritative sources of GAAP.) Companies that have not previously followed TIS 5100, paragraphs 38–76, will have to adopt that guidance on a prospective basis for revenue transactions entered into or materially modified in fiscal years on or after December 15, 2009, and interim periods within those years.

The Codification has been designed to present all of the authoritative accounting and financial reporting literature in a single, integrated offering using an online, real-time database. It reorganizes the pronouncements into about 90 accounting topics and displays all topics with in a consistent structure. It also includes relevant SEC guidance that follows the same topical structure in separate sections in the Codification. The FASB has been careful to state that the Codification doesn't change GAAP and that the project's goal was not to create any new GAAP. However, as noted above, the FASB has added selected items to the Codification that did not previously exist in the authoritative standards, which will, indeed, create GAAP in limited situations.

## Moving from an Audit Focus to an Entity Focus

The pre-Codification GAAP hierarchy has been subject to certain criticisms, not the least of which is the ranking of FASB Statements of Financial Accounting Concepts (SFACs) relative to that of GAAP and industry practice since the latter category receives no due process consideration while SFACs are subject to the same level of due process as that of FASB SFAS. The SEC also noted that the existing hierarchy was too complex, and was addressed to auditors instead of the entity. In making these observations, the SEC recommended FASB improve the GAAP hierarchy.

With the Codification, the GAAP hierarchy has been shifted from an auditor focus to an entity focus. Prior to the issuance of FASB Statement No. 162, *The Hierarchy of Generally Accepted Accounting Principles* in May 2008, GAAP for non-governmental entities had been established by an auditing standard, Statement on Auditing Standards (SAS) No. 69, *The Meaning of "Present Fairly in Conformity with Generally Accepted Accounting Principles."* These two standards divide GAAP into two tiers—Tier 1 (Accounting Principles) and Tier 2 (Other Authoritative Accounting Literature). In March 2009, the FASB issued a proposed Standard,

*The Hierarchy of Generally Accepted Accounting Principles—a Replacement of FASB Statement No. 162.* The proposal will replace the four levels of the GAAP hierarchy in SFAS No. 162 with just two levels—authoritative and non-authoritative. Authoritative sources will be contained in the Codification, while non-authoritative sources won't.

The significant differences and similarities between the two standards are as follows:

- SEC rules, interpretive releases and Staff Accounting Bulletins continue to be classified as category (A) GAAP for SEC registrants. Note that FASB EITF Abstracts (EITF D-Topics) are category (A) for SEC registered companies and category (C) for non registered companies.
- SFAS No. 162 adds FASB Statement No. 133, *Implementation Issues* and FASB Staff Positions in category (A) of Tier 1. These items were not included in SAS No. 69 category (A).
- Category (B) and category (C) are the same for both SAS No. 69 and SFAS No.162.
- AICPA Industry Audit and Accounting Guides and Statement of Position not cleared by the FASB are specifically included in category (D) by SFAS No. 162; however, they are not addressed in SAS No. 69. Otherwise, category (D) is the same for both SAS No. 69 and SFAS No. 162.
- The classifications A through D indicate the relative importance of a standard with category (A) being the most authoritative, then category (B), etc.
- The following table compares the provisions of SAS No. 69 with SFAS No. 162 to highlight the similarities and differences between the two statements.

**Tier 1 Accounting Principles**

<b>SAS No. 69</b>	<b>SFAS No. 162</b>
Hierarchy of GAAP Under SAS 69 for Nongovernmental Entities	SFAS No. 162, The Hierarchy of GAAP
<b>Category (A)</b>	<b>Category (A)</b>
FASB Statements of Financial Accounting Standards and Interpretations	FASB Statements of Financial Accounting Standards and Interpretations
AICPA Accounting Research Bulletins	AICPA Accounting Research Bulletins not superseded by action of the FASB
Accounting Principles Board (APB) Opinions	Accounting Principles Board (APB) Opinions not superseded by actions of the FASB FASB Statement 133 Implementation Issues FASB Staff Positions
SEC (Securities and Exchange Commission) Staff Accounting Bulletins and other Rules and Interpretations	SEC (Securities and Exchange Commission) Staff Accounting Bulletins and other Rules and Interpretations
<b>Category (B)</b>	<b>Category (B)</b>
FASB Technical Bulletins and AICPA Industry Audit and Accounting Guides and Statements of Position that have been cleared by FASB	FASB Technical Bulletins and AICPA Industry Audit and Accounting Guides and Statements of Position that have been cleared by FASB
<b>Category (C)</b>	<b>Category (C)</b>
AICPA Accounting Standards Executive Committee (AcSEC) Practice Bulletins cleared by the FASB and consensus positions of the FASB Emerging Issues Task Force (EITF)	AICPA Accounting Standards Executive Committee (AcSEC) Practice Bulletins cleared by the FASB and consensus positions of the FASB Emerging Issues Task Force (EITF), and topics discussed in Appendix D of EITF Abstracts
<b>Category (D)</b>	<b>Category (D)</b>
AICPA accounting interpretations and implementation guides (Q&As) published by the FASB staff and widely recognized industry or general practices	AICPA accounting interpretations and implementation guides (Q&As) published by the FASB staff, AICPA Industry Audit and Accounting Guides and Statements of Position not cleared by the FASB, and widely recognized industry or general practices

### Tier 2 Other Authoritative Accounting Literature

<b>SAS No. 69</b>	<b>SFAS No. 162</b>
FASB Statements of Financial Accounting Concepts	FASB Statements of Financial Accounting Concepts
AICPA Issue Papers	AICPA Issue Papers
Accounting Standards of the International Accounting Standards Committee	Accounting Standards of the International Accounting Standards Committee
Statements, Interpretations, and Technical Bulletins of the Governmental Accounting Standards Board (GASB)	
Statements, Interpretations, and Technical Bulletins of the Federal Accounting Standards Advisory Board (FASAB)	
Pronouncements of other professional associations or regulatory agencies	Pronouncements of other professional associations or regulatory agencies
AICPA Technical Practice Aids and Technical Information Service Inquires and Replies	AICPA Technical Practice Aids and Technical Information Service Inquires and Replies
Accounting textbooks, handbooks and articles	Accounting textbooks, handbooks and articles

## Reorganization and Codification

FASB and its consultants designed an online, searchable database it calls the FASB Accounting Standards Codification™ Research System (FASCRS) which includes a web-browser based interface optimized for use with either Microsoft Internet Explorer 6 and up and Firefox 2 and up (Mac users can use Firefox to access the tool). The thousands of pages of previous GAAP have been reorganized into approximately 90 topics.



## What's Included in the Codification

The Accounting Standards Codification (ASC) includes all levels (A) through (D) GAAP issued by standard-setters. It excludes standards applicable to state and local governmental units. To the extent not superseded by subsequent standards, the content included in the ASC includes:

Standard Setter	Common Acronym	Type of Standard
AICPA Committee on Accounting Procedure (CAP) (1939-1959)	ARB	Accounting Research Bulletins
AICPA Accounting Principles Board (APB) (1962-1973)	APB	Opinions
AICPA	AIN	Accounting Interpretations
	SOP	Statements of Position
	AAG	Audit and Accounting Guides (only incremental GAAP guidance)
	PB	Practice Bulletins
	TIS	Technical Inquiry Service (only with respect to Software Revenue Recognition)
Financial Accounting Standards Board (FASB) (1973–?)	FAS	Statements
	FIN	Interpretations
	FTB	Technical Bulletins
	FSP	Staff Positions
	Q&A	Staff Implementation Guides
	—	FAS 138 Derivatives Examples
FASB Emerging Issues Task Force (EITF) (1984–?)	EITF	Consensuses
	D	Appendix D Topics
FASB Derivatives Implementation Group (DIG)	DIG	Issues

The project team responsible for the ASC used, as the initial starting point, the “as-amended” versions of the standards as they existed as of June 1, 2007. Thus, if a particular authoritative document was issued for the sole purpose of amending a previously issued standard, the subsequent standard is not identified or cross-referenced since its effects had already been reflected in codifying the standard that it amended.

The Codification is generally comprised of the authoritative literature included in levels (A) through (D) of the current GAAP hierarchy as follows:

- Financial Standards Board (FASB)
  - Statements (FAS)
  - Interpretations (FIN)
  - Technical Bulletins (FTB)
  - Staff Positions (FSP)
  - Staff Implementation Guides (Q&A)
- Emerging Issues Task Force (EITF)
  - Abstracts
  - Appendix D Topics
- Derivative Implementation Group (DIG) Issues
- Accounting Principles Board (APB) Opinions
- Accounting Research Bulletins (ARB)
- Accounting Interpretations (AIN)
- American Institute of Certified Public Accountants (AICPA)
  - Statements of Position (SOP)
  - Audit and Accounting Guides (AAG)—only incremental accounting guidance
  - Practice Bulletins (PB)
  - Technical Inquiry Services (TIS)—only for Software Revenue Recognition

As a result, the Codification is made up of a smorgasbord of pronouncements issued by various standard-setting bodies over the years. The Codification also includes selected content issued by the SEC. However, the SEC content isn’t a complete representation of all rules, regulations, and other guidance relevant to public companies and does not replace or amend any guidance issued by the SEC or its staff.

## **What Does It Cost?**

The basic version of ASC is free. Most CPA firms, however, will want to purchase the “professional view.” The professional version includes advanced text searching and a cross-reference function. The cost of the professional view is \$850 per single concurrent user.

The FASB has said that they plan to issue a paper version of the Codification. No price has been established for the print version at this time. The FASB will evaluate whether to print future editions of the Codification based on the demand for the printed version.

## What's Not Included?

The ASC is not the official source of SEC guidance and does not contain the entire population of SEC rules, regulations, interpretive releases and staff guidance. Also, the ASC does not include governmental accounting standards.

- It is important to note that the FASB has not included some standards in their entirety. They identified some content included in the standards as nonessential content and, therefore, has excluded it from the Codification. Examples of such nonessential content include summaries of existing standards and summaries of constituent feedback.
- The Codification doesn't include standards for state and local governments. It also excludes guidance included in Level (E) of the previous GAAP hierarchy, such as accounting textbooks and articles. In developing the Codification, the FASB used a target effective date of December 31, 2008. Accordingly, the Codification excludes certain content that was superseded or outdated on December 31, 2008.
- The FASB also excluded from the Codification certain items referred to as "grandfathered materials." That includes guidance such as pooling of interests in a business combination, stock compensation for nonpublic entities, and pension transition assets or obligations.
- The ASC also does not include guidance for non-GAAP items such as OCBOA, Cash Basis, Income Tax Basis, and Regulatory Accounting Principles.

As part of the FASB's streamlining efforts, amending standards will be incorporated into amended standards. Standards that served merely to amend other standards have been eliminated.

## How Is It Organized?

The Codification is generally organized in a hierarchical structure by topic, subtopic, section, and subsection. Therefore, under each topic, there may be multiple subtopics, which may, in turn, have multiple sections and subsections beneath them. Each topic, subtopic, and section is assigned a specific numeric code. Topics are the broadest categorization of content and represent a collection of related guidance. The paragraph level in the hierarchical structure is where the actual topical content is located. All of the other elements in the Codification structure serve to focus selection to the paragraph level. All authoritative GAAP issued by the FASB will be issued in this format regardless of the form in which such guidance has been issued in the past.

The Codification includes a cross-reference report that identifies where current standards reside in the Codification or the source of material that is included in the Codification.

## Topical Organization

### **Numbering Conventions**

The ASC database is organized into the following broad topic areas:

1XX	General Principles and Objectives
2XX	Presentation
3XX	Assets
4XX	Liabilities
5XX	Equity
6XX	Revenue
7XX	Expenses
8XX	Broad Transactions
9XX	Industry
	Master Glossary
	Post-Codification Standards (with Basis for Conclusions)
	Exposure Drafts

### **High-Level Topic Areas**

#### General Principles and Objectives

- 105 Generally Accepted Accounting Principles
- 110 Placeholder for Conceptual Framework (not yet included in Codification)

#### Presentation

- 205 Presentation of Financial Statements
- 210 Balance Sheet
- 215 Statement of Shareholder Equity
- 220 Comprehensive Income
- 225 Income Statement
- 230 Statement of Cash Flows
- 235 Note to Financial Statements
- 250 Accounting Changes and Error Corrections
- 255 Changing Prices
- 260 Earnings per Share
- 270 Interim Reporting
- 272 Limited Liability Entities
- 275 Risks and Uncertainties
- 280 Segment Reporting

#### Assets

- 305 Cash and Cash Equivalents
- 310 Receivables
- 32X Investments
  - 320 Debt and Equity Securities
  - 323 Equity Method and Joint Ventures
  - 325 Other
- 330 Inventory
- 340 Deferred Costs and Other Assets
- 350 Intangibles-Goodwill and Other
- 360 Property, Plant and Equipment

Liabilities

- 405 Liabilities
- 410 Asset Retirement and Environmental Obligations
- 420 Exit or Disposal Cost Obligations
- 430 Deferred Revenue
- 440 Commitments
- 450 Contingencies
- 460 Guarantees
- 470 Debt
- 480 Distinguishing Liabilities from Equity

Equity

- 505 Equity

Revenue

- 605 Revenue Recognition

Expenses

- 705 Cost of Sales and Services
- 71X Compensation
  - 710 General
  - 712 Nonretirement Postemployment Benefits
  - 715 Retirement Benefits
  - 718 Stock Compensation
- 720 Other Expenses
- 730 Research and Development
- 740 Income Taxes

Broad Transactions

- 805 Business Combinations
- 810 Consolidation
- 815 Derivatives and Hedging
- 820 Fair Value Measurements and Disclosures
- 825 Financial Instruments
- 830 Foreign Currency Matters
- 835 Interest
- 840 Leases
- 845 Nonmonetary Transactions
- 850 Related Party Disclosures
- 852 Reorganizations
- 855 Subsequent Events
- 860 Transfers and Servicing

Industries

- 905 Agriculture
- 908 Airlines
- 910 Contractors-Construction
- 912 Contractors-Federal Government
- 915 Development Stage Entities
- 92X Entertainment
  - 920 Broadcasters
  - 922 Cable Television

924	Casinos
926	Film
928	Music
9XX	Extractive Activities
930	Mining
932	Oil and Gas
9XX	Financial Services
940	Brokers and Dealers
942	Depository and Lending
944	Insurance
946	Investment Companies
948	Mortgage Banking
950	Title Plant
952	Franchisors
954	Health Care Entities
958	Not-for-Profit Entities
96X	Plan Accounting
960	Defined Benefit Pension Plans
962	Defined Contribution Pension Plans
965	Health and Welfare Benefit Plans
97X	Real Estate
970	General
972	Common Interest Realty Associations
974	Real Estate Investment Trusts
976	Retail Land
978	Time-Sharing Activities
980	Regulated Operations
985	Software
995	U.S. Steamship Entities

### ***Paragraph Structure***

Each topic included in the database is organized consistently using the following numbering conventions (the first three digits correspond to the topic areas listed above):

### - ## - 00	Status
### - ## - 05	Overview and Background
### - ## - 10	Objectives
### - ## - 15	Scope and Scope Exceptions
### - ## - 20	Topical Definitions-Glossary
### - ## - 25	Recognition
### - ## - 30	Initial Measurement
### - ## - 35	Subsequent Measurement
### - ## - 40	Derecognition
### - ## - 45	Other Presentation Matters
### - ## - 50	Disclosure
### - ## - 55	Implementation Guidance and Illustrations
### - ## - 60	Relationships
### - ## - 65	Transition and Open Effective Date Information
### - ## - 70	Links to Grandfathered Material
### - ## - 75	XBRL Definitions (Reserved for future use)
### - ## - S##	Selected Incremental SEC Guidance

## Example of Hierarchical Organization

The chart below illustrates how to “drill down” into ASC detail on a particular topic as well as how to use the numeric structure of topics, subtopics, sections, and paragraph numbers to reference the ASC when documenting the results of accounting research.

Using the convention of preceding a citation to the FASB Accounting Standards Codification™ with the acronym, “ASC” as shown below is recommended.

Level	Example Caption	Example Cite
Overall Category	Expenses	
Topic	Income Taxes	ASC 740
Subtopic	Overall	ASC 740-10
Section	Other Presentation Matters	ASC 740-10-45
Subsection (not numbered)	General	
Paragraph Group 1	> Statement of Financial Position Classification of Income Tax Accounts	
Paragraph Group 2	> > Deferred Tax Accounts	
Paragraph Group 3	> > > Deferred Tax Accounts Related to an Asset or Liability	
Paragraph	Numbered, uncaptioned paragraph	740-10-45-7

## Securities and Exchange Commission Supplemental Guidance

To enhance the usability of the ASC for public companies, the ASC includes selected content issued by the SEC and its staff such as:

1. Regulation S-X (SX)
2. Financial Reporting Releases (FRR) and Accounting Series Releases (ASR)
3. Interpretive Releases (IR)
4. SEC Staff Guidance included in—
  - a. Staff Accounting Bulletins (SAB)
  - b. EITF Topic D comments by the SEC Staff Observer

The SEC guidance is organized in a similar topical hierarchy as the other guidance in the ASC using unique section codes preceded with the letter “S” in order to clearly differentiate it from the guidance applicable to all entities.

FASB was careful to caution the user, in its *Notice to Constituents* that accompanies the ASC, that the SEC sections do not contain all of the Commission’s rules, regulations, interpretations, and staff guidance. The ASC also does not contain the text of major securities statutes such as the Securities Act of 1933, the Securities Exchange Act of 1934, or the Sarbanes-Oxley Act

of 2002. The ASC also does not include SEC materials with respect to content included in regulatory filings that would be outside of the basic financial statements such as Management's Discussion and Analysis (MD&A). Since the scope of the ASC is limited to accounting matters, SEC guidance with respect to auditing and independence were also excluded from its content.

For those companies not subject to SEC reporting, the ASC Research System permits the user to exclude SEC content from views.

## Drafting Conventions

In committing to the ASC, the Financial Accounting Foundation intended that FASB would:

- Eliminate the confusing multi-tiered GAAP hierarchy.
- Use consistent grammatical construction and syntax.

Due to the fact that the content being codified was written by so many different parties over such a long period of time, it was important that, to the extent possible, the codified text be constructed using common grammatical and structural conventions to ease the process of reading, researching, understanding, and applying the guidance. The conventions used in the ASC include:

- The term "entity" is used instead of such comparable terms as—
  - Company
  - Enterprise
  - Organization
  - Firm
- The term "intra-entity" is used instead of intercompany.
- The term "shall" is used to refer to GAAP requirements instead of such terms as "should" or "must." It is important to note that this convention differs from the convention used in audit, attest, compilation, and review literature which uses "must" or "is required" to describe procedures deemed mandatory.
- "Would" and "should" are used in the implementation guidance and illustrations to refer to hypothetical situations.
- Generic qualifiers such as usually, ordinarily, and generally are avoided in the codification as FASB believes that they added ambiguity.
- Footnotes included in original pronouncements are avoided by incorporating the relevant text within the body of the discussion.
- Paragraphs containing lists are split out into a numbered hierarchy instead of being embedded within a paragraph.
- Although many of the legacy standards did not set forth their objectives, to the extent such objectives are stated, they are set off in boldfaced text to provide emphasis. FASB has committed to continuing this practice going forward to converge with this convention, which is used by the International Accounting Standards Board (IASB).



The ASC uses the following acronyms within its body. Any other acronym is defined in the glossary, referenced to the corresponding, spelled-out term.

<b>Acronym</b>	<b>Definition</b>
CD	Certificate of deposit
CUSIP	The nine-character unique alphanumeric identifier used in North America to identify securities for trading and clearing purposes
EPS	Earnings per share
FDIC	U.S. Federal Deposit Insurance Corporation
FIFO	First-in, first-out
FNMA	Federal National Mortgage Association
FHLMC	Federal Home Loan Mortgage Corporation (commonly referred to as “Freddie Mac”)
GAAP	Generally accepted accounting principles
GNMA	Government National Mortgage Association
IRS	Internal Revenue Service
LIBOR	London Interbank Offered Rate
LIFO	Last-in, first-out
LOCOM	Lower of cost or market
MD&A	Management discussion and analysis
NFP	Not-for-profit
SEC	Securities and Exchange Commission
VIE	Variable interest entity

The results of the behind-the-scenes buildout of the project were introduced to the accounting community in January 2008 at the web address <http://asc.fasb.org>. The primary purpose of that introduction was to provide adequate time for preparers, auditors, and academics to provide feedback regarding whether the content, as codified in the ASC, was faithful to the original pronouncements from which it was derived. This process is critical to project success since FASB’s intent was not to change the meaning or application of previously issued technical pronouncements.

## Grandfathered Material

### Previously Superseded Standards

Certain standards that have been superseded in the past were replaced with new standards that were to be applied prospectively to transactions occurring after the new standard's effective date. Thus, for transactions pre-dating the new standard, the entity was to continue to follow the authoritative guidance that had previously been in effect. The initial release of the ASC does not contain this grandfathered material and the researcher will need to continue to refer to the original pronouncements to access that guidance. After the July 1, 2009 date on which the ASC became authoritative, subsequent releases will populate, by relevant topic, any applicable grandfathered materials. Examples of grandfathered material excluded from the initial ASC release follows.

Description of Grandfathered Material	Pronouncement Originally Included In
1. Pooling of interests in a business combination.	FAS 141, ¶B217
2. Qualifying special-purpose entities (QSPEs).	FAS 140, ¶¶25 and ¶341
3. Pension transition assets or obligations.	FAS 87, ¶77
4. Employee Stock Ownership Plan (ESOP) shares purchased by, and held as of 12/31/1992.	SOP 93-6
5. Loans restructured in a troubled debt restructuring prior to the effective date of FAS 114.	FAS 118, ¶24
6. Stock compensation for nonpublic and other entities.	FAS 123(R), ¶83
7. Investment company investments acquired prior to 3/28/2002, or those acquired after 3/27/2002, pursuant to an irrevocable binding commitment existing prior to 3/28/2002.	AAG-Investment Companies, ¶1.05

### Other Grandfathered Standards

Prior to adoption of the ASC, FAS 162, *The Hierarchy of Generally Accepted Accounting Principles* governed the authoritative status of GAAP literature. That standard permitted entities that, as of March 15, 1992, had followed, and, subsequent to that date, have continued to follow accounting treatments previously in category (C) or category (D) of that hierarchy, to retain those accounting policies and not be required to change to accounting specified in higher categories (B) or (C) of that hierarchy if those standards in (B) or (C) had been effective prior to March 15, 1992.

For pronouncements with effective dates subsequent to March 15, 1992, and for entities initially applying an accounting principle after March 15, 1992, the following provisions apply:

- If the pronouncement was not an EITF pronouncement, entities are to follow the post-March 15, 1992 pronouncement, as codified in the ASC, for pre-existing transactions as well as for initial adoption of an accounting principle.
- EITF Consensuses became effective in the prior GAAP hierarchy for initial application of an accounting principle occurring after March 15, 1993.

## **Post-implementation Changes, Due Process, and Transitional Guidance**

Future changes will be proposed in documents consisting of two parts:

1. The text of the standard.
2. An appendix of ASC updating instructions showing how the standard would change the ASC using markup conventions (e.g., strikeout for deleted text and underlining for added text).

During the period between the date that a standard is approved and the date it becomes fully effective, the ASC will display it as “Pending Text” and will display it along with the existing content. The pending text will be accompanied by a link to any applicable transition guidance included in the new standard.

Once the new standard is fully effective, the outdated text will be removed from the paragraph and only the amended text will remain. The outdated text will be moved to a retrievable archive so that it can be accessed in future periods for research purposes.

In the future, new rules will come in the form of “Codification updates,” which will include the text to be replaced in order to highlight the changes. FASB intends to update the ASC concurrently with the release of a Codification Update.

## **FASB Statement No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles*, a replacement of FASB Statement No. 162 (ASC 105)**

### **Project Objectives**

- To rescind FAS 162 (the previous GAAP hierarchy).
- To adopt the FASB Accounting Standards Codification™ (ASC) as the single source of authoritative accounting principles for nongovernmental entities.

### **Effective Date and Transition Provisions**

The new FASB is effective for financial statements issued for interim and annual periods ending after September 15, 2009, except for certain nonpublic entities that had not adopted the revenue recognition guidance in AICPA Technical Inquiry Service Section 5100, “Revenue Recognition.” However, all entities—including the limited exception stated above—are required to adopt FASB No. 168 for periods beginning on or after December 15, 2009.

Although FASB's intent was not to change accounting guidance, to the extent that adoption of the ASC results in an accounting change, management is to determine whether the change is considered a change in accounting principle or a correction of a prior period error. In either case, the necessary accounting and disclosure guidance from what will be the former FAS 154, *Accounting Changes and Error Corrections* (ASC 250) is to be applied, as applicable, including disclosure of the accounting treatment prior to application and the reasons why application resulted in the change.

## Scope

This statement applies to financial statements of nongovernmental entities that are presented in conformity with U.S. GAAP.

## Background and Summary of Key Provisions

Upon adoption of the ASC, all previously issued standards were rescinded, as was the former hierarchy of GAAP. There are now only two levels of GAAP:

1. **Authoritative** – The FASB Accounting Standards Codification™ is the sole source of authoritative U.S. GAAP to be applied by nongovernmental entities, other than the rules and interpretive releases of the U.S. Securities and Exchange Commission (SEC), which, under the federal securities laws are statutorily considered authoritative sources of GAAP for SEC registrants. All guidance contained in the ASC carries an equal level of authority.
2. **Nonauthoritative** – Nonauthoritative literature includes:
  - a. FASB Statements of Financial Accounting Concepts.
  - b. International Financial Reporting Standards (IFRS) of the International Accounting Standards Board (IASB).
  - c. AICPA Issues Papers.
  - d. AICPA Technical Information Service (TIS) inquiries and replies included in the publication, *AICPA Technical Practice Aids*.
  - e. Pronouncements of other professional associations or regulatory agencies.
  - f. Practices that are widely recognized and prevalent (either generally or in the industry).
  - g. Accounting textbooks, handbooks, and articles.

In evaluating the appropriateness of nonauthoritative guidance, due consideration is to be given to the relevance to the particular circumstances, the specificity of the guidance, and the general recognition of the issuer or author as an authority.

Under d. above, FASB codified as authoritative GAAP TIS § 5100, paragraphs 38 through 76 in ASC 855-10-60; ASC 985-605-15, ASC 985-605-55, ASC 985-845-25, and ASC 985-845-55. All other TIS issues are considered nonauthoritative.

With respect to c. above, the following is a list of AICPA Issues Papers that have not been superseded or incorporated in other literature since their original issuance by the Accounting Standards Division of the AICPA.

<b>Title</b>	<b>Date Issued</b>
Accounting for Changes in Estimates	12/15/78
Accounting for Allowances for Losses on Certain Real Estate and Loans and Receivables Collateralized by Real Estate	6/21/79
Joint Venture Accounting	7/17/79
Accounting by Investors for Distributions Received in Excess of Their Investment in a Joint Venture (An addendum to the 7/17/79 Issues Paper on Joint Venture Accounting)	10/8/79
“Push Down Accounting”	10/30/79
Accounting in Consolidation for Issuances of a Subsidiary Stock	6/30/80
Certain Issues That Affect Accounting for Minority Interest in Consolidated Financial Statements	3/17/81
Depreciation of Income Producing Real Estate	11/16/81
The Acceptability of “Simplified LIFO” for Financial Reporting Purposes	10/14/82
Accounting for Employee Capital Accumulation Plans	11/4/82
Computation of Premium Deficiencies in Insurance Enterprises	3/26/84
Accounting by Stock Life Insurance Companies for Annuities, Universal Life, and Related Products and Accounting for Nonguaranteed-Premium Products	11/5/84
Identification and Discussion of Certain Financial Accounting and Reporting Issues Concerning LIFO Inventories	11/30/84
Accounting for Loss Portfolio Transfers—Letter	1/16/85
Accounting for Options	3/6/86
The Use of Discounting in Financial Reporting for Monetary Items With Uncertain Terms Other Than Those Covered by Existing Authoritative Literature	9/9/87
Quasi Reorganizations	10/28/88

## When GAAP Is Silent

Under the proposal, if guidance relevant to a transaction or event is not specified within a source of authoritative GAAP for that entity, management is to consider authoritative GAAP that would be applicable to that entity for similar transactions or events. If no such guidance can be found, management would then consider nonauthoritative guidance from other sources. Management is precluded from applying an accounting treatment specified for similar transactions or events when the accounting principles describing that treatment either prohibit the application of those principles to the particular transaction or event, or prohibit application of that accounting treatment by analogy.

## Migration of Accounting Rules Contained in Auditing Literature

While the ASC was not intending to change GAAP, there are two notable exceptions. Historically, the provisions of GAAP that dealt with going concern and subsequent events have resided in the auditing literature. Since these matters both have financial reporting repercussions, FASB decided they should be migrated to GAAP literature.

## Future Codification Updates

In the future, all new standards the FASB issues will include two parts: the Standard, and the Codification Update Instructions. New standards issued in the future by the FASB will not be considered authoritative in themselves but will serve only to update the Codification and provide background information and bases for conclusions on the changes made in the Codification.

## Implementing the Codification

The first step in implementing the new Codification is learning how to use the system. The FASB has several options for training on how to use the Codification. They offer an online tutorial. This tutorial can be accessed at **[www.fasb.org](http://www.fasb.org)**. In addition, an archived webcast is available that provides step-by-step instructions.

The home page at **<http://asc.fasb.org>** includes various documents that users may find helpful including a “Notice to Constituents” that describes various Codification-related matters. It also includes general information about how to use the online research system and special features like the *Cross Reference Reports* that can be used to locate where standards are housed.

When preparing to implement the new Codification, consider the following recommendations to ensure a smooth transition to the new way of researching accounting standards:

- Be sure that your staff is trained on the use of the new Codification system. The key to successfully implementing the ASC is adequate training.
- Ensure that your firm is referencing the FASB ASC in all of its policies and procedures manuals.
- Determine which is the first set of financial statements that will need to reflect the ASC changes.
- Review how you are accounting for certain transactions to be sure that any changes resulting from the ASC have not caused you to improperly account for the transactions.

## SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

1. Which of the following groups is most affected by the FASB Codification?
  - a. IASB.
  - b. Accountants.
  - c. SEC.
  - d. Tax preparers.
2. Which of the following is **not** cited in the text as having opposed financial reporting changes proposed by the FASB in the years prior to Enron's collapse?
  - a. Congress.
  - b. Large public accounting firms.
  - c. Public companies.
  - d. AICPA.
3. According to the text, what "buzzword" was often used when discussing ways to fix the reporting system?
  - a. Transparency.
  - b. SPEs.
  - c. Enron.
  - d. Andersen.
4. Who authorized the Codification?
  - a. SOX.
  - b. PCAOB.
  - c. AICPA.
  - d. FAF.
5. What was the effective date of the Accounting Standards Codification?
  - a. January 2008.
  - b. January 2009.
  - c. April 2009.
  - d. July 2009.

6. Which of the following shifted the GAAP hierarchy from an audit focus to an entity focus?
  - a. FASB Statement No. 133.
  - b. FASB Statement No. 162.
  - c. SAS No. 69.
  - d. SAS No. 95.
7. Where did SAS No. 69 rank EITFs within the pre-ASC GAAP hierarchy?
  - a. Category A.
  - b. Category B.
  - c. Category C.
  - d. Category D.
8. FASB Statements of Financial Accounting Concepts are found under which category of the pre-ASC GAAP hierarchy?
  - a. Category A.
  - b. Category B.
  - c. Category D.
9. Which of the following is included in the ASC?
  - a. All FASB standards in their entirety.
  - b. Pension transition assets or obligations.
  - c. Superseded content as of December 31, 2008.
  - d. Selected content issued by the SEC.
10. Which of the following is one of the ways in which ASC meets current needs for authoritative guidance?
  - a. ASC is the single source of GAAP guidance for public companies.
  - b. ASC is the sole GAAP authority for governmental operations.
  - c. Amending standards will be incorporated into amended standards.
  - d. The AICPA has sole authority for maintaining GAAP standards.



11. In the ASC codification structure, which of the following numbered elements contains the topical content?
- a. Area.
  - b. Topic.
  - c. Subsection.
  - d. Paragraph.
12. Which of the following topics have been migrated from the auditing literature to GAAP?
- i. Going concern
  - ii. Subsequent events
  - iii. Qualifying special purpose entities (QSPEs)
  - iv. Loans restructured in a trouble debt restructuring prior to the effective date of FAS 114.
  - v. Presentation of financial statements.
- a. v.
  - b. i, ii.
  - c. iii, iv.



## SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

1. Which of the following groups is most affected by the FASB Codification? **(Page 1)**
  - a. IASB. [This answer is incorrect. The IASB is not affected by the FASB ASC, because it is an international organization.]
  - b. **Accountants. [This answer is correct. ASC is the single source of U.S. GAAP for accountants.]**
  - c. SEC. [This answer is incorrect. The SEC sets standards for publicly traded companies only, therefore is only partially affected by the ACS.]
  - d. Tax preparers. [This answer is incorrect. Tax preparers are generally not affected by the Codification since they do not prepare financial statements.]
2. Which of the following is **not** cited in the text as having opposed financial reporting changes proposed by the FASB in the years prior to Enron's collapse? **(Page 1)**
  - a. Congress. [This answer is incorrect. Congress put pressure on FASB to back down on some of its proposed changes and eventually, the FASB did back down.]
  - b. Large public accounting firms. [This answer is incorrect. The large public accounting firms kept their opposition low key, but wrote letters to the FASB expressing their opposition to certain proposed changes in reporting.]
  - c. Public companies. [This answer is incorrect. Corporate America opposed the FASB's proposed changes and some public companies staged public protests in opposition to rule changes proposed by the FASB during the 1990's.]
  - d. **AICPA. [This answer is correct. The AICPA was not one of the entities that opposed the FASB's proposed standards changes although they did comment on them.]**
3. According to the text, what "buzzword" was often used when discussing ways to fix the reporting system? **(Page 2)**
  - a. **Transparency. [This answer is correct. There was a perceived need for transparency in financial statements to prevent future occurrences of failures such as Enron and WorldCom.]**
  - b. SPEs. [This answer is incorrect. SPE is an acronym for special-purpose entity. SPEs were one of the vehicles used by Enron to cloud their financial picture, but it was not the word cited in the text as being used when discussing ways to fix the reporting system.]
  - c. Enron. [This answer is incorrect. Enron was a major failure early in this decade, but it was not the word cited in the text as being used when searching for solutions to problems in the financial reporting system.]
  - d. Andersen. [This answer is incorrect. Arthur Andersen became a poster child for conflicts of interest in the public accounting profession, but it was not the word cited in the text as being used when discussing ways to improve the financial reporting system.]

4. Who authorized the Codification? **(Page 2)**
- a. SOX. [This answer is incorrect. SOX pertains to public companies only, and is not affected by ASC.]
  - b. PCAOB. [This answer is incorrect. The PCAOB sets standards for registered public accounting firms involving audit reports of public companies. The PCAOB is not responsible for ASC.]
  - c. AICPA. [This answer is incorrect. The AICPA is not responsible for ASC and could not, therefore, authorize the project.]
  - d. **FAF. [This answer is correct. Authorization for the Codification was given by the Trustees of the Financial Accounting Foundation, the FASB's oversight board.]**
5. What was the effective date of the Accounting Standards Codification? **(Page 3)**
- a. January 2008. [This answer is incorrect. This is the date on which the verification period began.]
  - b. January 2009. [This answer is incorrect. This is the date on which the verification period ended.]
  - c. April 2009. [This answer is incorrect. This was originally intended as the implementation date, but the date was changed.]
  - d. **July 2009. [This answer is correct. The ASC was effective July 1, 2009.]**
6. Which of the following shifted the GAAP hierarchy from an audit focus to an entity focus? **(Page 3)**
- a. FASB Statement No. 133. [This answer is incorrect. FASB Statement No. 133 relates to the implementation issues but does not shift the GAAP hierarchy.]
  - b. **FASB Statement No. 162. [This answer is correct. FASB Statement No. 162, *The Hierarchy of GAAP*, shifted the focus of GAAP from an auditor focus to an entity focus.]**
  - c. SAS No. 69. [This answer is incorrect. SAS No. 69, *The Meaning of Presents Fairly in Conformity with GAAP*, made GAAP auditor focused rather than entity focused.]
  - d. SAS No. 95. [This answer is incorrect. SAS No. 95 is the standard addressing audit standards not accounting standards.]
7. Where did SAS No. 69 rank EITFs within the pre-ASC GAAP hierarchy? **(Page 5)**
- a. Category A. [This answer is incorrect. Even though some EITFs have been subjected to FASB due process, they are not ranked on Level A.]
  - b. Category B. [This answer is incorrect. Level B is reserved for FASB Technical Bulletins and certain "FASB cleared" guidance, not EITFs.]
  - c. **Category C. [This answer is correct. Before SFAS 162, SAS 69 ranked all EITF guidance on Level C.]**
  - d. Category D. [This answer is incorrect. Prior to SFAS 162, SAS 69 ranked AICPA accounting interpretations and implementation guides published by the FASB staff on Level D.]

8. FASB Statements of Financial Accounting Concepts are found under which category of the pre-ASC GAAP hierarchy? **(Page 5)**
- a. Category A. [This answer is incorrect. Although FASB SFACs are subject to FASB due process, they are not found under Category A of the pre-ASC GAAP hierarchy.]
  - b. Category B. [This answer is incorrect. Category B of the pre-ASC GAAP hierarchy is reserved for certain “FASB cleared” guidance such as AICPA SOPs.]
  - c. **Category D. [This answer is correct. Although FASB SFACs are subject to FASB due process, they are found on the lowest level, Category D of the pre-ASC hierarchy, as part of the body of “other relevant accounting literature.” The pre-ASC hierarchy has been criticized for its ranking of SFACs.]**
9. Which of the following is included in the ASC? **(Page 9)**
- a. All FASB standards in their entirety. [This answer is incorrect. FASB identified some content included in the standards as nonessential content and therefore, excluded it from the Codification. Examples are summaries of existing standards and summaries of constituent feedback.]
  - b. Pension transition assets or obligations. [This answer is incorrect. The FASB excluded “grandfathered materials” from the Codification. Examples include guidance on pooling of interests in a business combination, stock compensation for nonpublic entities, and pension transition assets or obligations.]
  - c. Superseded content as of December 31, 2008. [This answer is incorrect. FASB used a target effective date of December 31, 2008, when developing the Codification, thus the Codification excludes certain content that was superseded or outdated on December 31, 2008.]
  - d. **Selected content issued by the SEC. [This answer is correct. The Codification doesn’t include the entire population of SEC rules, regulations, interpretive releases and other guidance relevant to public companies.]**
10. Which of the following is one of the ways in which ASC meets current needs for authoritative guidance? **(Page 9)**
- a. ASC is the single source of GAAP guidance for public companies. [This answer is incorrect. Although certain SEC guidance is included in ASC, the SEC, not the ASC, is the authoritative source of guidance for public companies.]
  - b. ASC is the sole GAAP authority for governmental operations. [This answer is incorrect. ASC does not include governmental accounting standards.]
  - c. **Amending standards will be incorporated into amended standards. [This answer is correct. As part of its streamlining efforts, FASB eliminated standards that served merely to amend other standards by incorporating the changes into the standards being amended.]**
  - d. The AICPA has sole authority for maintaining GAAP standards. [This answer is incorrect. The authority does not lie with the AICPA, but with the FASB.]

11. In the ASC codification structure, which of the following numbered elements contains the topical content? **(Page 9)**
- a. Area. [This answer is incorrect. The Area is the first level of ASC organization, but is not a numbered part of the codification structure.]
  - b. Topic. [This answer is incorrect. The Topic is the first element of the codification structure, but does not contain topical content.]
  - c. Subsection. [This answer is incorrect. Subsections occur only occasionally; they are not numbered and do not contain topical content.]
  - d. **Paragraph. [This answer is correct. Paragraphs are the last element of the codification structure and contain the actual topical content. All other elements of the codification structure serve to focus selection to the paragraph level.]**
12. Which of the following topics have been migrated from the auditing literature to GAAP? **(Page 20)**
- i. Going concern
  - ii. Subsequent events
  - iii. Qualifying special purpose entities (QSPEs)
  - iv. Loans restructured in a trouble debt restructuring prior to the effective date of FAS 114
  - v. Presentation of financial statements
- a. v. [This answer is incorrect. Presentation of financial statements is subtopic 205 under the broad topic of Presentation in the ASC. It never resided exclusively in the auditing literature.]
  - b. **i, ii. [This answer is correct. Historically, the provisions of GAAP that dealt with going concern and subsequent events were found in the auditing literature. Since both have financial reporting repercussions, FASB decided to migrate them to GAAP literature.]**
  - c. iii, iv. [This answer is incorrect. QSPEs and loans restructured in a trouble debt restructuring prior to the effective date of FAS 114, are both examples of grandfathered material that was excluded from the ASC. Neither were migrated from the auditing literature to GAAP.]

## EXAMINATION FOR CPE CREDIT

### Lesson 1

Determine the best answer for each question below. Then log onto our Online Grading Center at **OnlineGrading.Thomson.com** to record your answers.

1. Which of the following organizations is most directly affected by ASC?
  - a. GASB.
  - b. SEC.
  - c. IASC.
  - d. FASB.
2. What does the acronym "ASC" stand for?
  - a. American Standards Codification.
  - b. Accounting Standards Codification.
  - c. American Standard Codes.
  - d. Accounting Standard Codes.
3. Which of the following was **not** under criticism and review after Enron collapsed?
  - a. FASB.
  - b. POB.
  - c. IASC.
  - d. PCAOB.
4. Which of the following statements is correct?
  - a. The FASB is both an authoritative and a regulatory body.
  - b. FASB's existence was reportedly at risk after Enron's collapse.
  - c. Congress disbanded the POB prior to enacting SOX.
  - d. International convergence was cited as one reason for Enron's collapse.
5. Who is overseeing the ASC project?
  - a. FASB.
  - b. EITF.
  - c. APB.
  - d. AcSEC.

6. When was the ASC project approved?
  - a. Circa 2001.
  - b. Circa 2004.
  - c. Circa 2008.
  - d. Circa 2009.
7. How many levels of the pre-ASC GAAP hierarchy are considered authoritative?
  - a. Three.
  - b. Four.
  - c. Five.
  - d. Six.
8. How many levels of the ASC GAAP hierarchy are considered authoritative?
  - a. One.
  - b. Two.
  - c. Three.
  - d. Four.
9. ASC streamlines GAAP by organizing authoritative pronouncements into approximately how many topics?
  - a. 50.
  - b. 90.
  - c. 1,000.
  - d. 2,000.
10. Which of the following statements is correct concerning the interaction between ASC, XBRL, and IFRS?
  - a. ASC is the first step in the preparation for convergence with IFRS.
  - b. ASC codes will be updated for XBRL taxonomies once XBRL is official.
  - c. Between XBRL and ASC, XBRL is controlling.
  - d. IFRS will make only marginal use of XBRL.
11. Which of the following statements is correct concerning ASC organization and structure?
  - a. ASC reorganizes Levels A through C of the GAAP hierarchy.
  - b. ASC summarizes GAAP into five areas of subject matter.
  - c. ASC refers to GAAP by a code composed of five distinct elements.
  - d. ASC denotes SEC guidance with an “S” prefix.



## Lesson 2: Codification and Convergence

### Learning Objectives

Completion of this lesson will enable you to:

- Identify differences between IFRS and U.S. GAAP.
- Identify ongoing developments as FASB and IASB standards converge under the Memorandum of Understanding (MoU) between the two Boards.

### Introduction

As far back as 1979, the SEC, upon its adoption of Form 20-F, the basic disclosure document for foreign private issuers, expressed its aspiration for the “harmonization of international disclosure standards.” In 1988, the SEC issued a policy statement on the regulation of international securities markets in which it noted that the “ultimate goal should be the development of an integrated international disclosure system.”

The U.S. share of the market capitalization of worldwide capital markets is currently less than half. Based on statistics published by the World Federation of Exchanges, as of December 31, 2008, the market cap of listed stocks on the major exchanges was distributed globally as follows (in trillions of U.S. Dollars—“USD”):

<b>Geographic Location</b>	<b>Market Cap of Listed Equity in USD Trillions</b>	<b>% of Total</b>
United States	\$11.605	47%
Canada	1.033	4
Europe	6.029	25
Asia	<u>5.870</u>	<u>24</u>
	<u>\$24.537</u>	<u>100%</u>

Prior to the current distressed economic conditions, there had been a trend of explosive growth rates in countries such as Brazil, India, Korea, Singapore, and China, to name a few. While the current distressed worldwide economy may derail this growth, it is likely to resume as economic conditions improve.

Concerns are arising in U.S. political and economic circles that the U.S. regulatory environment, subsequent to the enactment of the Sarbanes-Oxley Act of 2002 (along with the litigious nature of our culture), may be making it less attractive for companies to seek listing on our stock exchanges, which they may view as cost-prohibitive.

Additionally, as markets have globalized, there are now unprecedented opportunities for U.S. investors to diversify their portfolios by investing globally. The U.S. Bureau of Economic Analysis (part of the U.S. Department of Commerce) estimates that U.S. residents had collectively increased their investments in foreign equity securities from \$200 billion in 1990 to \$4.3 trillion in 2006.

In order to provide those investors with timely, complete, reliable and comparable financial information on which to base their decision making, a common global accounting platform will become a necessity.

Given the trends cited above, former SEC Chairman, Christopher Cox made it a high priority to pursue the elimination of barriers to U.S. capital markets. During his tenure as Chairman, supervisory arrangements for enforcement and regulatory cooperation were entered into with the SEC's counterpart regulators in the United Kingdom, France, the Netherlands, Belgium, Portugal, Australia, Germany, Bulgaria and Norway.

In his role as the Chairman of the Technical Committee of the International Organization of Securities Commissions (IOSCO), he advocated for the convergence of U.S. GAAP and IFRS. In December 2007, the SEC adopted rules that permitted foreign issuers to list on U.S. exchanges using IFRS without reconciling between IFRS and GAAP as had been previously required. This development, more than any other, contributed to calls from many commentators, to level the playing field by allowing domestic filers the same ability to use IFRS for the purpose of regulatory filings as their foreign counterparts.

Chairman Cox's successor, Mary L. Schapiro was unanimously confirmed by the Senate on January 22, 2009 and is the first woman to chair the Commission. On January 15, 2009, during her confirmation hearings, she gave testimony before the Senate Committee on Banking, Housing and Urban Affairs that, to say the least, appeared to distance herself from the IFRS Roadmap. The transcript of those hearings included the following response to a question posed by Senator Jack Reed (D-RI):

I would proceed with great caution so that we don't have a race to the bottom. I think we all can agree that a single set of accounting standards used around the world would be a very beneficial thing, [would] allow investors to compare companies around the world. That said, I have some concerns about the road map that has been published by the SEC and is out for comment now, and I have some concerns about the IFRS standards generally. They are not as detailed as the U.S. standards. There's a lot left to interpretation. Even if adopted, there will still be a lack of consistency, I believe, around the world in how they are implemented and how they are enforced.

The cost to switch from U.S. GAAP to IFRS is going to be extraordinary, and I've seen some estimates that range as high as \$30 million for each U.S. company in order to do that. This is a time when I think we have to think carefully about whether imposing those sorts of costs on U.S. industry, really make sense. And perhaps my greatest concern is the independence of the International Accounting Standards Board and the ability to have oversight of their process for setting accounting standards and the amount of rigor that exists in that process today. So, I will tell you that I will take a big deep breath and look at this entire area again, carefully, and will not necessarily feel bound by the existing road map that's out for comment.

The following section of this course summarizes the "roadmap" proposed by the SEC. It should be read in the context that it is a nonbinding Concepts Release meant to elicit comments from market participants and constituents, and that there is a high degree of uncertainty regarding its future.

## The Proposed SEC “Roadmap”

### ***Recent Developments—SEC Release Nos. 33-9109; 34-61578***

On February 23, 2010, the SEC reaffirmed its commitment to the convergence of U.S. GAAP and IFRS.

After consideration of comment letters received, the Commission directed the staff to develop a Work Plan, the results of which will aid the Commission in evaluating the effect of IFRS on financial reporting by U.S. companies. The Work Plan will address six areas of concern:

- Sufficient development and application of IFRS for the U.S. domestic reporting system
- The independence of standard setting for the benefit of investors
- Investor understanding and education regarding IFRS
- Examination of the U.S. regulatory environment that would be affected by a change in accounting standards
- The impact on issuers, both large and small, including changes to accounting systems, changes to contractual arrangements, corporate governance considerations, and litigation contingencies
- Human capital readiness

Public progress reports on the Work Plan will be available beginning in October 2010. By 2011, the Commission will decide whether to incorporate IFRS into the U.S. financial reporting system, and if so, when and how. If the Commission determines in 2011 to incorporate IFRS into the U.S. financial reporting system, the first time U.S. companies would report under such a system would be no earlier than 2015.

The SEC has withdrawn the proposed rules to allow early adoption of IFRS and is not currently pursuing an early use option. Also, they are not ruling out the possibility of permitting issuers to choose between IFRS and GAAP.

### ***SEC Release No. 33-8982, Proposed Rule: Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers***

On November 14, 2008, the SEC issued Release 33-8982, *Roadmap for the Potential use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers*. The SEC stated that “this Roadmap sets forth several milestones that, if achieved, could lead to the required use of IFRS by U.S. issuers in 2014 if the Commission believes it to be in the public interest and for the protection of investors.” The SEC also is proposing to allow early use of IFRS by a limited number of U.S. issuers if the issuer’s industry uses IFRS as the basis of financial reporting more than any other set of standards.

Under the Release, the SEC in 2011 will determine whether to proceed with rulemaking to require U.S. issuers to use IFRS beginning in 2014.

## ***Proposed Scope and Scope Exceptions***

The proposed roadmap relates solely to U.S. issuers with respect to their periodic reporting requirements under Sections 13 and 15(d) of the Exchange Act, proxy and information statements under Section 14 of the Exchange Act and registration statements under Section 12 of the Exchange Act and Section 7 of the Securities Act. The roadmap does not contemplate adoption of IFRS by investment companies regulated under the Investment Company Act of 1940 (15 USC § 80), or by regulated entities such as registered broker-dealers.

## ***Summary of Key Provisions of the Proposal***

### **The Seven Milestones**

The stated objective of the roadmap is to provide investors with financial information from U.S. issuers using a set of high-quality; globally accepted accounting standards that will enable them to better compare financial information of U.S. issuers and competing international investment opportunities. It is further intended to encourage market participants to consider the effect of IFRS on U.S. capital markets and to prepare for the use of IFRS financial statements by U.S. issuers in their filings with the SEC.

The Roadmap uses a “milestone-based” approach. It contains specific milestones that must be achieved in order for the SEC, in 2011, to go forward with a decision to mandatorily adopt IFRS for all domestic public registrants over the phased implementation timetable included in the proposal. This aspect of the proposal has been the subject of much criticism due to:

- The subjectivity of assessing whether the vaguely worded “milestones” are actually accomplished.
- The deferral of a decision regarding a “date certain” on which registrants would be required to adopt IFRS.
- The complex approach to be followed by registrants eligible to elect early adoption along with the risks that, if they should make the election, those companies might be required to switch back to U.S. GAAP if all of the milestones are not met.

In effect, the roadmap doesn't lead to a destination, it is only a commitment to defer a final decision to a later date.

The seven milestones set forth in the roadmap are as follows.

### ***Milestone 1: Improvements to IFRS***

The SEC will consider the extent of progress made by the FASB and the IASB on their joint work plan under the updated Memorandum of Understanding (abbreviated as the “MoU” or referred to as the “Norwalk Agreement”). The SEC encourages both boards to continue working toward completion of the projects included in that work plan so that, by 2011, the SEC will be able to judge the IFRS framework to be of high quality and sufficiently comprehensive for use in the United States.

In addition to evaluating improvements in the IFRS standards, the SEC also will evaluate whether improvements are made to the process followed to set those standards.

### ***Milestone 2: Accountability and funding of the IASC Foundation***

The London-based IASB is currently subject to oversight by the IASC Foundation, a stand-alone, not-for-profit organization based in London and incorporated in Delaware. The Foundation is governed by 22 trustees with geographically diverse backgrounds.

Financing for IASB operations is predominantly provided by voluntary contributions from accounting firms, companies, international organizations, central banks, and governments.

The SEC has expressed legitimate concerns regarding the independence of the IASB under the current funding mechanism and will closely monitor the efforts of the Foundation to obtain a secure, stable funding mechanism that supports the independent functioning of the IASB.

In addition, to improve the accountability of the IASB, the IASC Foundation Trustees have proposed amendments to its Constitution to provide accountability to a Monitoring Group composed of securities authorities that would be charged with participating in and approving nominations for IASC Foundation Trustees, reviewing funding arrangements for adequacy and appropriateness, and addressing matters that the IASC Foundation Trustees are responsible for, such as oversight of the IASB and potential areas for consideration by the IASB as it conducts its ongoing work.

### ***Milestone 3: Improvement of the Ability to Use Interactive Data for IFRS Reporting***

In order to ensure that, under IFRS, U.S. issuers would continue to be able to report using eXtensible Business Reporting Language (XBRL), the SEC will consider progress made on the state of development of IFRS taxonomies prior to proceeding with rulemaking on IFRS for all U.S. issuers.

### ***Milestone 4: Education and Training***

Critical to a successful implementation of this magnitude, is the ability to effectively train a wide group of stakeholders involved in the entire financial statement chain of distribution. The wide range of stakeholders includes, but is not limited to:

- |                                   |                         |
|-----------------------------------|-------------------------|
| • Academicians/Educators          | • Investment Managers   |
| • Actuaries                       | • Individual Investors  |
| • Analysts, Internal and External | • Issuer Personnel      |
| • Attorneys                       | • Lenders               |
| • Audit Committees                | • Pension Plan Trustees |
| • Boards of Directors             | • Ratings Agencies      |
| • CPE Developers and Instructors  | • Statement Preparers   |
| • Customers                       | • Sureties              |
| • Government Agencies             | • Valuation Experts     |
| • Internal and External Auditors  | • Vendors               |

Professional associations and industry groups would need to integrate IFRS into their training materials, publications, testing, and certification examinations, including the Uniform CPA Examination.

***Milestone 5: Limited Early Use of IFRS Where it Would Enhance Comparability for U.S. Investors***

As previously described, the SEC believes that the limited early use of IFRS by eligible electing companies will provide valuable information to those issuers that would be scheduled to adopt IFRS at a later date.

***Milestone 6: Anticipated Timing of Future Rulemaking by the SEC***

To assist the SEC in its decision whether to mandate the use of IFRS by U.S. issuers, it would direct the Office of the Chief Accountant, with appropriate consultation with other SEC Divisions and Offices, to undertake a study and report to the SEC on the implications for investors and other market participants of the implementation of IFRS for U.S. issuers. The SEC anticipates that it would make the resulting report public.

The SEC Staff has commenced a comprehensive review of all SEC rules relating to financial reporting in order to recommend amendments that would fully implement IFRS reporting throughout its regulatory framework for reporting under the Exchange Act and the Securities Act.

After reviewing the status of the milestones and the results of the study, the SEC would decide in 2011, whether to proceed with rules that would require U.S. public companies to file financial statements in accordance with IFRS starting in 2014. This step would only be taken if the SEC believed that it would promote investor protection and be in the public interest.

Should the SEC choose to proceed with rulemaking for the mandatory use of IFRS by all U.S. issuers, it would continue to require that issuers provide three years of audited financial statements prepared using IFRS. Thus, the large accelerated filers that would begin reporting under IFRS in 2014 would be required to file financial statements for 2012, 2013, and 2014 with the SEC.

The proposed Roadmap expresses the SEC's belief that action in 2011 would provide issuers with sufficient early notice of the transition to IFRS to permit them to begin their internal accounting using IFRS in 2012, which would be the earliest fiscal year covered under the earliest anticipated phase-in for IFRS reporting in 2014. Given the enormity of the task for some companies, this is highly debatable.

***Milestone 7: Implementation of the Mandatory Use of IFRS by U.S. Issuers***

The proposed Roadmap suggests a staged, mandatory transition that would commence in 2014 and result in all U.S. issuers covered by the scope of the Roadmap being IFRS-compliant by 2016. By basing the phase-in on the definitions of accelerated filer and large accelerated filer under the Exchange Act, which classifies issuers based on the size of the worldwide public float of their equity securities, the SEC believes that those most able to commit the resources to the conversion would be able to meet the earliest phase-in date. The SEC further believed that, by staging the transition, it would help manage resource demands on auditors, consultants and other market participants.



The Roadmap does acknowledge, however, that staging the transition in this manner does result in some noncomparability of financial information. Further, by basing the staging on issuer size, that noncomparability would exist among issuers within an industry. The staging of the transition would also temporarily create a dual reporting system for U.S. issuers that would require investor familiarity with both IFRS and U.S. GAAP.

Among the issues the SEC will consider in 2011 when making its decision, would be expanding the eligibility criteria to include additional U.S. issuers that would be eligible to voluntarily elect to use IFRS in their filings prior to the mandatory transition date.

## **Other Considerations**

### ***Effects on Other Reporting Requirements***

Various issuers are subject to requirements of federal and state regulators in addition to the SEC. Regulators of financial institutions, insurance companies, and public utilities require periodic financial information on an ongoing basis. For example, U.S. GAAP financial statements are frequently used as a basis for determining capital requirements for financial institutions. Absent changes to these regulators' requirements, affected issuers might be required to maintain two sets of records to enable reporting under both IFRS and U.S. GAAP.

The Internal Revenue Code (IRC) contains LIFO inventory conformity provisions that require taxpayers that elect the last-in, first-out method of inventory valuation to use that method to value inventories in their basic, general-purpose financial statements. Since IFRS does not permit the use of LIFO, issuers converting to IFRS would be required to terminate their LIFO election and pay income taxes on the recapture of the "LIFO reserve." Absent a legislative change in the IRC, this could cause affected U.S. issuers to incur substantial additional income taxes.

Many U.S. companies have issued debt securities under indentures or have entered into loan agreements that contain various covenants based upon financial measurements such as a stated minimum tangible net worth. These contractual obligations may explicitly require the use of U.S. GAAP in connection with the computation of compliance with those financial covenants or for the purpose of submitting financial reports. This could potentially have an adverse effect on these issuers unless the legal agreements are amended to permit IFRS measurement and reporting.

Some widely referenced market indices, such as the S&P 500, currently only include issuers that file their financial statements using U.S. GAAP. Absent any changes in these indices, IFRS reporting could affect an issuer's ability to be included in such indices or financial instruments based on those indices. This could potentially have an adverse effect on these issuers, unless changes are made to the indices.

### ***Accounting Systems, Controls and Procedures***

Converting to IFRS would require issuers to make changes to their financial reporting systems including manual and automated controls, and related policies and procedures. Depending on the complexity of issuer's business activities, geographical reach, reporting structure, and transaction cycles, these changes can be quite extensive and costly, and require a substantial amount of lead time to design, build, test, and implement.

Many complications can arise in converting from U.S. GAAP to IFRS. In preparing IFRS financial statements, an issuer would be required to obtain IFRS-compliant financial information about its equity method investees in order to properly record its share of the investee's earnings for each period presented. If that investee did not report using IFRS, it would prove both difficult and costly for the issuer to obtain the necessary information.

Costs and complications would also arise with respect to private companies wanting to file an initial public offering (IPO). If the private company had previously been reporting under U.S. GAAP, as would undoubtedly be the case in most situations, substantial costs would be incurred to provide IFRS-compliant audited financial statements for the purposes of the initial registration statement to be filed with the SEC.

### **Auditing**

Needless to say, cost and complexity will be associated with the process of independent auditors<sup>1</sup> integrated audits of the issuer's financial statements and the effectiveness of the issuer's internal control over financial reporting. For those firms that have less global reach than firms referred to as the "Big 4" and "second tier" firms, this may be especially challenging. Such firms are likely to have fewer resources available to them through affiliated or network firms located in jurisdictions in which issuers are already reporting in accordance with IFRS. The SEC expressed its concern that this could contribute to increased concentration in the auditing profession, which has been a major public policy concern since the demise of Andersen in the wake of the Enron and WorldCom debacles.

Audit firms that recently made changes to their systems of quality control to implement Statement of Quality Control Standards No. 7, *A Firm's System of Quality Control* would need to consider additional changes to the elements of their quality control systems especially as they relate to the Human Resources element in areas such as:

- Recruitment and hiring
- Determining capabilities and competencies
- Assigning personnel to engagements, *and*
- Professional development

There is widespread concern in the profession regarding the availability of an adequate supply of properly trained and educated auditors in order to meet the auditing needs inherent in the Roadmap's timetable. The Roadmap proposal expresses this concern:

U.S. audit firms may encounter challenges in establishing policies and procedures, and hiring and training personnel, to provide themselves with reasonable assurance that their personnel would possess knowledge appropriate to perform audits of U.S. issuers.

One potential audit complication cited by the proposed Roadmap relates to an auditor's ability to issue an opinion of IFRS financial statements due to application of the IFRS standard on contingencies. Under that standard, an issuer would be required to record a contingent liability with respect to litigation when it is more likely than not (MLTN) that an obligation exists. This MLTN threshold would result in liabilities being recorded under IFRS that would not be

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<sup>1</sup> Referred to under PCAOB standards as "registered public accounting firms" due to the requirement that they register with the PCAOB and are subject to its discipline and inspection protocols.



recorded under the less stringent requirements of U.S. GAAP. Concerns have been raised regarding an auditor's ability to corroborate the information furnished by management related to litigation, claims, and assessments by obtaining an audit inquiry letter from a client's attorney. This could open up a contentious dialogue between accountants and lawyers as it might necessitate changes to the longstanding statement of policy referred to as the "American Bar Association Statement of Policy Regarding Lawyer's Responses to Auditors' Requests for Information" (also commonly referred to as the "Treaty").<sup>2</sup>

The Roadmap indicates that additional guidance would most likely be necessary from the PCAOB and that the PCAOB would need to amend references to U.S. GAAP that exist in their current standards.

### ***The State of IFRS***

In addition to seeking achievement of the "milestones," the SEC expects to consider, among other things, whether IFRS as issued by the IASB is a globally accepted set of accounting standards and whether it is consistently applied across companies, industries, and countries.

Concerns expressed in the proposed roadmap include:

- The lack of prescriptive, rules-based guidance and safe harbors that have been so prevalent under U.S. GAAP.
- The lesser amount of detailed implementation guidance included in IFRS and the effect this might have on consistency, auditors' legal liability, and the outcomes of discussions between management and auditors with respect to particular accounting treatments. There might also be a lesser ability on the part of the enforcement arms of the SEC and PCAOB to predict the outcomes of enforcement actions they choose to undertake.
- The effect on comparability of the greater "optionality" allowed under IFRS to elect different methods of accounting for similar transactions.
- The lack of guidance in IFRS for certain specific types of industries or transactions including:
  - Insurance contracts.
  - Extractive activities.
  - Certain common control transactions.
  - Recapitalizations.
  - Reorganizations.
  - Acquisitions of minority shares not resulting in a change of control and similar transactions.

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<sup>2</sup> See AU §337C.

- The lack of uniform, worldwide adoption of IFRS as issued by the IASB has been especially problematic. Different countries have adopted internal processes through which they adopt or incorporate IFRS into their national accounting standards on a standard-by-standard basis. Decisions made during those processes may result in those national accounting standards containing discrepancies from IFRS as issued by the IASB. These are referred to as “jurisdictional variants” of IFRS and they undermine the worldwide comparability of financial reporting. A notable example of this problem is the process followed in the European Union (EU). While the EU has adopted most of the IFRSs, the process of adoption can cause time lags. In addition, the EU modified IAS 39, *Financial Instruments: Recognition and Measurement* in adopting it, thus causing differences between how it is applied in the EU and how it is applied elsewhere. The EU also permits separate company financial statements to be issued in accordance with “IFRSs as adopted in the EU” even though their issuance is contradictory to IAS 27, *Consolidated and Separate Financial Statements* as issued by the IASB.

This “as-endorsed” versus “as-issued” approach may result in pressure on the IASB in the development of its standards. In addition, the need for the IASB to obtain consensus from such a diverse range of constituents could cause a lengthening of the time it takes to deliberate and issue new standards.

- The SEC also cites a concern regarding the reduction of influence that the U.S. and its capital markets would have over the process of standards-setting. The SEC’s participation in the oversight of the IASB would be through its participation in a proposed Monitoring Group. This would, of course, result in less direct oversight than the SEC currently has over the FASB.
- IFRS 7, *Financial Instruments: Disclosure* (as recently amended) requires disclosure in the notes to the financial statements of sensitivity analysis based on forward-looking information. U.S. issuers are currently subject to Item 305 of Regulation S-K (17 CFR 229.3-05) which requires quantitative and qualitative disclosures about market risk with respect to certain financial instruments. That information, however, is not included in the financial statements of the filing and, to the extent that the information constitutes forward-looking statements, is expressly subject to statutory safe harbors provided under Section 27A of the Securities Act (15 USC 77z-2) and Section 21E of the Exchange Act (15 USC 78u-5).

The cited safe harbors do not apply to information appearing in the notes to audited financial statements. Obviously, this is a matter of great concern for management and the issuer’s auditors.

## **IFRS for SMEs (International Financial Reporting Standards for Small and Medium-sized Entities)**

### **Issue date**

July 2009

### **Effective date**

Effective for financial statements issued upon adoption of the IFRS framework with a one year delay for implementation of the amendments to IFRS.

## Objectives

The objective of financial statements of small or medium-sized entities is to provide information about the financial position, performance, stewardship of management, and cash flows of the entity that is useful for economic decision-making by a broad range of external users. IFRS for SMEs focuses on the recognition, measurement, and disclosure principles critical to those entities.

## Scope

*IFRS for SMEs* is intended for use by entities that do not have public accountability and publish general purpose financial statements for external users. [Note: IFRS for SMEs is an acceptable framework for U.S. companies upon its effective date.]

## Background and Summary of Key Provisions

Global financial reporting standards, consistently applied, enhance the comparability of financial information and thereby improve the efficiency of the allocation and pricing of capital. SMEs can benefit from financial statements that are comparable from country to country in:

- Access to and pricing of cross-border borrowings.
- Access to and terms with vendors and suppliers.
- Developing uniform credit ratings.
- Access to and pricing of venture capital.
- Reporting to outside investors.

*IFRS for SMEs* is intended for entities that do not have public accountability: have not issued debt or equity securities in a public market; hold assets in a fiduciary capacity as its primary business, e.g., banks, insurance companies, broker/dealers, pension funds, mutual funds, investment banks. There is no size test in defining SMEs. A subsidiary of an entity may use *IFRS for SMEs* only if it also meets the public accountability test.

*IFRS for SMEs* is a complete, self-contained set of standards. Reference to any other reporting framework is inappropriate. An entity that elects to report under *IFRS for SMEs* must make an "explicit and unreserved" declaration to that effect in the notes to the financial statements. And the financial statements must comply with all relevant requirements of the standard.

The following table discusses the major differences in the recognition and measurement principles between IFRS and IFRS for SMEs.

Accounting Principle	IFRS for SMEs	IFRS
Noncurrent assets (or groups of assets and liabilities) held-for-sale	Holding assets for sale triggers an assessment for impairment.	IFRS 5: Measured at lower of carrying amount and fair value less costs to sell. Depreciation stops when classified as held-for-sale.
Unvested past service cost of defined benefit pension plans	Recognized in profit or loss immediately.	IAS 19: Recognized as an expense on a straight-line basis over the average period until the benefits become vested.
Exchange differences on a monetary item that forms part of the net investment in a foreign operation, in consolidated financial statements	Recognized in OCI and not reclassify in profit or loss on disposal of the investment.	IAS 21: Reclassify in profit and loss on disposal of the investment.
Borrowing costs	Charged to expense.	IAS 23: Capitalize costs directly attributable to the acquisition, construction, or production of qualifying assets.
Investment in an associate for which there is a published price	Measured at fair value through profit and loss.	IAS 28: Measured using the equity method.
Investment in a jointly controlled entity for which there is a published price	Measured at fair value through profit and loss.	IAS 31: Measured using the equity method or proportionate consolidation.
Investment property whose fair value can be measured reliably without undue cost or effort	Measured at fair value through profit and loss.	IAS 40: Choice of either fair value through profit or loss or cost-depreciation-impairment model.
Biological assets	Measured at fair value through profit and loss only if fair value is readily determinable without undue cost or effort.	IAS 41: Presumption that fair value can be readily measured.
Income tax	Where a different tax rate applies to distributed income, initially measure current and deferred taxes at the rate applicable to undistributed profits.	ED, Income Taxes: Initially measure current and deferred taxes at the tax rate expected to apply when the profits are distributed.
Share-based payments with cash alternatives in which the terms of the arrangement provide the counterparty with a choice of settlement	Account for the transaction as a cash-settled share-based payment transaction unless past practice settles the transaction by issuing equity instructions.	IFRS 2: Accounting for a compound instrument.

Accounting Principle	IFRS for SMEs	IFRS
Presentation simplification	<p>Not required to present a statement of financial position at the beginning of the earliest comparable period when applying an accounting policy retrospectively, or there is a retrospective restatement.</p> <p>All deferred tax assets and liabilities classified as noncurrent.</p> <p>Present a single statement of income and retained earnings in place of separate statements of comprehensive income and changes in equity if the only changes to equity arise from profit or loss, dividends, corrections of errors, and changes in accounting policy.</p>	<p>IAS 1: Requires.</p> <p>ED, Income Taxes: Classification as either current or noncurrent according to the classification of the related nontax asset or liability.</p> <p>Option not available.</p>
Disclosure simplification	<p>Earnings per share.</p> <p>Interim financial reporting.</p> <p>Segment reporting.</p> <p>Special accounting for assets held-for-sale.</p> <p>Financial instruments.</p> <p>Goodwill and other intangibles.</p> <p>Development costs.</p> <p>Income taxes.</p> <p>Employee benefit plans.</p> <p>Share-based payments.</p> <p>Investments and investment property.</p> <p>Government grants.</p> <p>Leases.</p> <p>No review of useful life, residual value and depreciation/ amortization method on a annual basis.</p> <p>Jointly controlled entities.</p> <p>Operating cash flows.</p>	

## **FASB Convergence Initiatives—The Norwalk Agreement/Memorandum of Understanding; Current Project Inventory**

In a joint meeting of the FASB and IASB in September 2002, the two Boards issued “The Norwalk Agreement” in which they mutually committed to the development of high-quality, compatible accounting standards that could be used to facilitate domestic and cross-border financial reporting. At that meeting the Boards pledged to use their best efforts to:

- Make their existing standards fully compatible as soon as was practically possible, and
- Coordinate their future technical agendas to ensure that once achieved, compatibility would be maintained.

It is important to note that the pledges made were drafted in a manner that suggests that the two Boards would continue to co-exist and that contains no hint that either of the Boards would ultimately be a globally accepted standard setter.

At various times in the ensuing years, the Boards reaffirmed their commitments and adjusted their agendas accordingly.

In February 2006, the Boards issued a Memorandum of Understanding (MoU) which set forth the relative priorities in their joint work programs. The MoU was based on three overriding principles:

1. Convergence of accounting standards is best achieved through the development, over time, of high-quality common standards,
2. Attempting to eliminate differences between two standards that are both in need of significant improvement is not the best use of either of the Boards’ resources; rather, a common standard should be developed that improves the information provided to investors, and
3. Serving investors’ needs means that the Boards should seek convergence by replacing standards in need of improvement with jointly developed new standards.

In 2007, based on its perception of the progress made by the Boards, the SEC removed its requirement that foreign companies registering securities in the U.S. reconcile financial statements prepared in accordance with IFRS as issued by the IASB to U.S. GAAP.

In September 2008, the Boards published an “agreed-upon pathway” describing their plans for completing the various projects that were the subject of the 2006 MoU. Notably, the timetable included in this “pathway” would result in completion of all of the major MoU projects by 2011, the year in which the SEC subsequently proposed, in its Roadmap document, to decide on whether to require U.S. issuers to convert to IFRS.

The current status of MoU and other joint FASB/IASB projects is set forth below. Consideration should be given, however, to recent economic developments and commitments made by FASB and IASB in response to the credit crisis as these matters are likely to cause revisions to the previously agreed-upon timetable.

<b>Project Description</b>	<b>Estimated Year of Issuance of Final Document</b>	<b>Joint, MoU, or Both?</b>
Consolidation	IASB-2010 FASB-Completed	Both
Derecognition of Financial Instruments	IASB-2010 FASB-Completed	Both
Emissions Trading Schemes	2011	Joint
Fair Value Measurement Guidance	IASB 2010 FASB - Completed	MoU
Financial Instruments	ASAP	MoU
Distinguishing Liabilities from Equity	2010	Both
Financial Statement Presentation	2011	Both
Income Taxes	Unknown	Both
Insurance Contracts	2011	Joint
Leases	2011	Both
Pensions/Post-employment Benefits	2011	MoU
Revenue Recognition	2011	Both
Discontinued Operations	2010	Joint
Earnings per Share	2010	Joint
Joint Ventures	2010	MoU
Joint Conceptual Framework	TBD	Joint

**Current Exposure Drafts:**

Financial Instruments: Amortized Cost and Impairment  
 Classification of Rights  
 Classification and Measurement  
 Impairment and Provisioning  
 Hedging—Embedded Derivatives  
 Improving Disclosures about Financial Instruments  
 Investments in Debt Instruments  
 Improvements to IFRSs  
 Discount Rate for Employee Benefit Plans  
 Classification of Rights Issues: Proposed Amendment to IAS 32

Rate-regulated Activities  
 Management Commentary  
 Statement of Comprehensive Income  
 Fair Value Measurement  
 Income Tax  
 Derecognition: Proposed Amendments to IAS 39 and IFRS 7  
 Amendments to IAS 23: Borrowing Costs  
 Amendments to IFRS 3, Business Combinations and IAS 27, Consolidated and Separate Financial Statements  
 Amendments to IAS 1: Presentation of Financial Statements

### Recently Completed Projects

Standard	Summary of Provisions
IFRS 1 Amendment: Exemption from Comparative IFRS 7 Disclosures	Exempts first time adopters of IFRSs from providing the additional disclosures in IFRS 7.
IFRIC 14 Amendment—IAS 19: The limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction	Corrects IFRIC 14 to allow recognition of prepayments for minimum funding contributions.
IFRS 9: Financial Instruments—Classification and Measurement of Financial Assets (Replacement for IASB 39)	<p>A financial asset or financial liability would be measured at amortized cost if: 91) the instrument has basic loan features; and (2) the instrument is managed on a contractual yield basis.</p> <p>Eliminates the classifications of "held to maturity" and "available for sale."</p> <p>Some equity investments may be measured at fair value through comprehensive income.</p> <p>Eliminates need for separate accounting for an embedded derivative.</p> <p>Prohibits reclassification of financial assets and financial liabilities after initial recognition.</p>
IAS 24: Related Party Disclosures	<p>Related party disclosures for:</p> <ul style="list-style-type: none"> <li>• Transactions between parents and subsidiaries.</li> <li>• Management compensation: short-term benefits, post-employment benefits, other long-term benefits, termination benefits, share-based payments.</li> <li>• Related party transactions: nature, amounts, balances, doubtful debts.</li> </ul>
IFRS 2: Share-based Payment Amendment (IFRICs 8 and 11 Withdrawn)	An entity that receives goods and services in a share-based payment arrangement must account for those goods or services no matter which entity in the group settles the transaction, and no matter whether the transaction is settled in shares or in cash.
IFRIC 9 and 16 Amendments	Amendment to the restriction on the entity that can hold hedging instruments.
IFRIC 17: Distribution of Noncash Assets to Owners	<p>A dividend payable is recognized when the dividend is authorized at the fair value of the net assets to be distributed.</p> <p>The liability is remeasured at each reporting date; changes recognized directly in equity.</p> <p>Differences between the dividend paid and the carrying amount of the net assets is distributed to profit and loss.</p>



Standard	Summary of Provisions
IFRIC 18: Transfers of Assets from Customers	<p>Recognize the transferred asset at fair value if the entity has control.</p> <p>Separately account for the multiple deliverables.</p>
IFRIC 19: Extinguishing Liabilities with Equity Instruments	<p>Debtor derecognizes the financial liability fully or partly.</p> <p>Equity issued is measured at fair value.</p> <p>If the liability is only partly extinguished, allocate the fair value between that which is extinguished and that retained. If there is substantial modification of the part remaining, the entire liability should be derecognized and a new liability recognized.</p> <p>Recognize profit and loss on the difference between the carrying amount of the debt extinguished and equity issued.</p>
IFRS 7 Amendment	Three level hierarchy for fair value measurement disclosures (same as Level I, II, III under SFAS No. 157).

## Other Ways that IFRS Is Gaining Traction in the U.S.

### The AICPA Council

The AICPA Council passed the following resolutions on May 18, 2008:

#### International Accounting Standards Board

RESOLVED: That the International Accounting Standards Board (IASB) is hereby designated as the body to establish professional standards with respect to international financial accounting and reporting principles pursuant to Rule 202 [ET § 202.01] and Rule 203 [ET § 203.01]; and

BE IT FURTHER RESOLVED: That the Council shall reassess, no sooner than three years but not later than five years after the effective date of this resolution, whether continued recognition of the IASB as the body designated to establish professional standards with respect to International financial accounting and reporting principles under Rule 202 and Rule 203 is appropriate.

Although, in recent years, the AICPA has diminished in influence and largely become a de facto trade association, the resolutions are significant because they enable members of the AICPA to be associated with and report on financial statements prepared in accordance with IFRS as issued by the IASB.

## **The Uniform CPA Examination**

At its October 17–18, 2008 meeting, the AICPA Board of Examiners (BOE) approved new Content and Skill Specification Outlines (CSOs/SSOs) which constitute statements of the knowledge and skills to be measured by the CPA Examination. These outlines are developed considering input from state boards of accountancy, the National Association of State Boards of Accountancy (NASBA), standard-setters, accounting firms, state CPA societies, the academic community, and individual CPAs. In addition, the BOE consults with psychometricians and other testing experts to ensure test validity.

The new CSOs include IFRS on the content and skills for the Financial Accounting and Reporting (FAR) section of the examination. IFRS will be tested beginning in January 2011.

## **Deliberations of the FASB Private Company Financial Reporting Committee (PCFRC) with Respect to Post-convergence Options for Nonissuers**

Needless to say, the vast majority of businesses in the U.S. are not issuers and do not file financial statements with the SEC. The likely waning influence of FASB that will result from eventual conversion of public companies to IFRS has the potential to create a financial reporting vacuum for private entities. As PCFRC monitors developments in the SEC roadmap comment process, it has issued a discussion document designed to facilitate a discussion of the various models that could potentially fill that vacuum.

In December 2009, the AICPA and the Financial Accounting Foundation formed a "blue-ribbon panel" to address how U.S. accounting standards can meet the needs of users of private company financial statements. That panel will provide recommendations to standard-setters after considering comments from a cross-section of financial reporting constituencies, including lenders, investors, owners, preparers, auditors, and regulators. The consideration of the effect of any convergence of an international financial reporting framework with U.S. generally accepted accounting principles is part of the charge of this group.

The following briefly summarizes those models considered by PCFRC.

### ***Model 1: IFRS with Private Entities Option***

All U.S. companies, public and private, would adopt IFRS as their accounting framework. Similar to companies in other countries, U.S. companies that do not have public accountability would have the option of following a simplified framework that the IASB issued in July 2009, which is referred to as IFRS for SMEs. If a company is not eligible to elect IFRS for SMEs, it would either follow full IFRS or, as is currently the case, elect to use an Other Comprehensive Basis of Accounting (OCBOA) such as the income tax basis or cash basis.

### ***Model 2: U.S. Adapted Version of IFRS for SMEs***

The IFRS for SMEs standard is tailored to meet the needs of private company financial reporting in the U.S.

### ***Model 3: IFRS with Differential Reporting***

The full IFRS framework as issued by the IASB is modified to meet the unique needs of U.S. private companies by deleting some requirements or embedding different treatments in the standards.

### ***Model 4: Separate U.S. Private Company GAAP—Revised***

Under this model, current U.S. GAAP would be reviewed, modified, and built out into a comprehensive, self-contained accounting standards framework suitable for private companies. The framework would be designed to be suitable for private companies with or without significant external financial statement users, and would be sensitive to the unique needs of owner-managed entities.

### ***Model 5: Separate U.S. GAAP, Maintained and Updated in the Future***

The full U.S. GAAP framework would continue to be maintained as it currently exists (the FASB Accounting Standards Codification™ (ASC) effective July 1, 2009) for continued use by private companies. The ASC, just as it is now, would be subject to periodic updating for needed changes and improvements while taking into account the standard setting activities of the IASB and emerging issues in the private company arena. This model does not call for the initial review and modification of current U.S. GAAP as described in Model 4.

Members of IFAC include both the AICPA and Canadian Institute of Chartered Accountants. In addition, IFAC is affiliated with the Institute of Internal Auditors (IIA) and the Information Systems Audit and Control Association (ISACA).

## **The International Federation of Accountants (IFAC), The Forum of Firms (FOF), and the Transnational Auditors Committee (TAC)**

### ***The International Federation of Accountants (IFAC)***

The International Federation of Accountants (IFAC) is the accounting profession's global organization. It has 157 members and associates in 122 countries and jurisdictions representing 2.5 million accountants employed in public practice, industry, commerce, government, and academia.

IFAC was founded in 1977 and its Secretariat is based in New York City. Its mission is to serve the public interest by strengthening the worldwide accountancy profession and contribute to the development of strong international economies by establishing and promoting adherence to high-quality professional standards, furthering the international convergence of those standards, and speaking out on public interest issues where the profession has unique, relevant expertise.

IFAC Boards and Committees are responsible for the following global standards.

Type of Standard	Issuing Body
International Standards on Auditing (ISA)	International Auditing and Assurance Standards Board (IAASB)
International Standards on Review Engagements (ISRE)	
International Standards on Quality Control (ISQC)	
International Standards on Assurance Engagements (ISAE)	
International Standards on Related Services (ISRS) [compilations and agreed-upon procedures with respect to financial information]	
International Public Sector Accounting Standards (IPSAS)	International Public Sector Accounting Standards Board
Code of Ethics for Professional Accountants (the "Code")	International Ethics Standards Board for Accountants (IESBA)
International Education Standards and International Education Practice Statements	International Accounting Education Standards Board (IAESB)

Members of IFAC include both the AICPA and Canadian Institute of Chartered Accountants. In addition, IFAC is affiliated with the Institute of Internal Auditors (IIA) and the Information Systems Audit and Control Association (ISACA).

### ***The Forum of Firms (FOF) and Transnational Auditors Committee (TAC)***

Many U.S. CPA firms are affiliated with global networks to enable them to extend their reach in servicing the increasingly globalized needs of their clients. In 2002, the Forum of Firms (FOF) was established as an association of international networks of accounting firms that perform audits of financial statements that are used, or could potentially be used across national borders.

The objective of the FOF is to promote consistent and high quality standards of financial reporting and auditing practices worldwide. The FOF brings together firms that perform transnational audits and involve them more closely with the activities of the International Federation of Accountants (IFAC) in audit and other assurance-related areas.

The Transnational Auditors Committee (TAC) is a committee of IFAC and serves as the executive arm of the FOF. Thus it provides the official linkage between IFAC and the FOF.

The FOF is registered as a legal entity in Switzerland and, as of January 2009, had 21 full members and 1 provisional member (Polaris International):

**Full Members**

- Baker Tilly International Limited
- BDO International
- Constantin Associates Network
- Deloitte Touche Tohmatsu
- Ernst & Young Global Limited
- Grant Thornton International Limited
- HLB International
- Horwath International
- IEC
- INPACT Audit Limited
- JHI
- KPMG International
- Mazars
- Moore Stephens International Limited
- PKF International Limited
- PricewaterhouseCoopers International
- RSM International Limited
- Russell Bedford International
- SMS Latinoamérica
- Talal Abu-Ghazaleh & Co. International
- UHY International Limited

To qualify to be a member of the FOF, a firm or network must meet the following criteria:

- Has been engaged or is interested in being engaged to perform transnational audits,
- Promotes the consistent application of high quality audit practices worldwide, including the use of International Standards on Auditing (ISAs),
- Supports convergence of national auditing standards with the ISAs, and
- Agrees to meet the FOF's membership obligations, listed below.

FOF member firms must meet the following membership obligations:

- Maintain appropriate quality control standards in accordance with International Standards on Quality Control (ISQC) issued by the International Auditing and Assurance Standards Board (IAASB) in addition to relevant national quality control standards,
- Conduct, to the extent not prohibited by national regulation, regular globally coordinated internal quality assurance reviews,
- Implement policies and methodologies for the conduct of transnational audits that are based, to the extent practical, on ISAs,
- Implement policies and methodologies that conform to the IFAC *Code of Ethics for Professional Accountants* and national codes of ethics, and
- Agree to submit an annual report to the FOF Secretary in a form approved by TAC, indicating that the membership obligations have been met.

Naturally, not all accounting firms that belong to the FOF member networks conduct transnational audits. Thus FOF members are charged with identifying to the FOF those firms that comprise their membership in the FOF. Thus, FOF member networks will have some member firms that are excluded from the network for FOF purposes. These are referred to as “correspondent firms.” All other firms that are identified as comprising the FOF membership are covered by the above criteria and bound by the above membership obligations.

Attest standards have already been revised to allow for the issuance of and reporting on financial statements using the IFRS framework.

## Appendix to—Map of FASB ASC to IFRS

The following comparison of U.S. GAAP and IFRS will show the differences and similarities of the two standards. FASB believes that one of the benefits of the structure of the ASC is that it more closely aligns with pronouncements of the International Accounting Standards Board (IASB). The following summarizes how U.S. GAAP contained in the ASC maps to the corresponding IASB pronouncements.

ASC Topic #	Topic	IFRS Pron.	IASB Pronouncement Title
105	Generally Accepted Accounting Principles	Preface	Preface to IFRSs
205	Presentation of Financial Statements	IAS 1	Presentation of Financial Statements
205–20	Presentation of Financial Statements—Discontinued Operations	IFRS 5	Non-current Assets Held for Sale and Discontinued Operations
210	Balance Sheet		
215	Statement of Shareholder Equity		
220	Comprehensive Income		
225	Income Statement		
230	Statement of Cash Flows	IAS 7	Statement of Cash Flows
235	Notes to Financial Statements		
250	Accounting Changes and Error Corrections	IAS 8 IFRS 1	Accounting Policies, Changes in Accounting Estimates and Errors First-time Adoption of International Financial Reporting Standards
255	Changing Prices	IAS 29	Financial Reporting in Hyperinflationary Economies
260	Earnings per Share	IAS 33	Earnings Per Share
270	Interim Reporting	IAS 34	Interim Financial Reporting
272	Limited Liability Entities		
275	Risks and Uncertainties		

<b>ASC Topic #</b>	<b>Topic</b>	<b>IFRS Pron.</b>	<b>IASB Pronouncement Title</b>
280	Segment Reporting	IAS 14 IFRS 8	Segment Reporting Operating Segments
305	Cash and Cash Equivalents		
310	Receivables		
320	Investments—Debt and Equity Securities		
323	Investments—Equity Method and Joint Ventures	IAS 28 IAS 31	Investments in Associates Interests in Joint Ventures
325	Investments—Other	IAS 40	Investment Property
330	Inventory	IAS 2	Inventories
340	Deferred Costs and Other Assets		
350	Intangibles—Goodwill and Other	IAS 38	Intangible Assets
360	Property, Plant, and Equipment	IAS 16 IAS 36	Property, Plant, and Equipment Impairment of Assets
405	Liabilities		
410	Asset Retirement and Environmental Obligations		
420	Exit or Disposal Cost Obligations		
430	Deferred Revenue		
440	Commitments		
450	Contingencies	IAS 37	Provisions, Contingent Liabilities, and Contingent Assets
460	Guarantees		
470	Debt		
480	Distinguishing Liabilities from Equity		
505	Equity		
605	Revenue Recognition	IAS18	Revenue
705	Cost of Sales and Services		
710	Compensation—General	IAS 19	Employee Benefits
712	Compensation—Nonretirement Postemployment Benefits		
715	Compensation—Retirement Benefits	IAS 26	Accounting and Reporting by Retirement Benefit Plans
718	Compensation—Stock Compensation	IFRS 2	Share—based Payment

<b>ASC Topic #</b>	<b>Topic</b>	<b>IFRS Pron.</b>	<b>IASB Pronouncement Title</b>
720	Other Expenses		
730	Research and Development		
731	Research and Development		
740	Income Taxes	IAS 12	Income Taxes
805	Business Combinations	IFRS 3	Business Combinations
810	Consolidation	IAS 27	Consolidated and Separate Financial Statements
815	Derivatives and Hedging		
820	Fair Value Measurements and Disclosures		
825	Financial Instruments	IAS 32 IAS 39 IFRS 7	Financial Instruments: Presentation Financial Instruments: Recognition and Measurement Financial Instruments: Disclosures
830	Foreign Currency Matters	IAS 21	The Effects of Changes in Foreign Exchange Rates
835	Interest	IAS 23	Borrowing Costs
840	Leases	IAS 17	Leases
845	Nonmonetary Transactions		
850	Related Party Disclosures	IAS 24	Related Party Disclosures
852	Reorganizations		
855	Subsequent Events	IAS 10	Events after the Reporting Period
860	Transfers and Servicing		
905	Agriculture	IAS 41	Agriculture
908	Airlines		
910	Contractors—Construction	IAS 11	Construction Contracts
912	Contractors—Federal Government		
915	Development Stage Entities		
920	Entertainment—Broadcasters		
922	Entertainment—Cable Television		
924	Entertainment—Casinos		
926	Entertainment—Films		
928	Entertainment—Music		
930	Extractive Activities—Mining	IFRS 6	Exploration for and Evaluation of Mineral Assets



<b>ASC Topic #</b>	<b>Topic</b>	<b>IFRS Pron.</b>	<b>IASB Pronouncement Title</b>
932	Extractive Activities—Oil and Gas		
940	Financial Services—Broker and Dealers		
942	Financial Services—Depository and Lending		
944	Financial Services—Insurance	IFRS 4	Insurance Contracts
946	Financial Services—Investment Companies		
948	Financial Services—Mortgage Banking		
950	Financial Services—Title Plant		
952	Franchisors		
954	Health Care Entities		
958	Not-for-profit Entities		
960	Plan Accounting—Defined Benefit Pension Plans		
962	Plan Accounting—Defined Contribution Pension Plans		
965	Plan Accounting—Health and Welfare Benefit Plans		
970	Real Estate—General		
972	Real Estate—Common Interest Realty Associations		
974	Real Estate—Real Estate Investment Trusts		
976	Real Estate—Retail Land		
978	Real Estate—Time-sharing Activities		
980	Regulated Operations		
985	Software		
995	U.S. Steamship Entities		
		IAS 20	Accounting for Government Grants and Disclosure of Government Assistance

## **Codification, Convergence and XBRL—The Perfect Storm?**

There are a lot of things that have to be accomplished before we will be able to have a redesigned GAAP codification system that possibly includes International Financial Reporting Standards that will permit the issuance of financial statements using XBRL. The new GAAP Codification is a reality and should improve financial reporting as it currently stands under U.S. GAAP and will significantly reduce the time and effort required to research GAAP issues. Implementing IFRS, however, is a more difficult proposition. There are so many issues that need to be addressed—will the U.S. fully adopt IFRS or only partially adopt the standards, will IFRS support XBRL reporting, and so on?

A more pressing problem relates to the new FASB Codification. The current XBRL taxonomy that is used to set tags corresponding to financial statement line items displays references to the accounting and regulatory rules applicable to that item. However, the current taxonomy uses the pre-codification organization of the FASB literature. A new taxonomy that references the new codification structure of the FASB GAAP Standards will be available in 2010.

Any issue caused by the adoption of IFRS is probably not going to impact the Codification since it is unlikely that IFRS will be adopted universally before 2015 if at all. There will be some cost involved in implementing the new Codification but this may be more than offset by the time saved when researching GAAP issues. XBRL may be an issue for public companies reporting in that time period before a new taxonomy has been put in place, so maybe that perfect storm will not be more than a summer rain.

## SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

13. Which of the following best describes the overarching reason for the convergence of FASB and IASB standards?
- a. Investment markets have become global.
  - b. The U.S. share of the worldwide capital markets has fallen to less than half.
  - c. The litigious culture of the U.S. has made it less attractive to companies seeking a stock exchange listing.
14. Your client is an investment company regulated under the Investment Company Act of 1940. Is your client included on the IFRS roadmap?
- a. Yes.
  - b. No.
15. The IFRS standards are expected to have effects on other reporting requirements. From the list below, select the reporting requirements that will be affected by IFRS.
- i. An issuer required to provide state regulators with a financial statement based on GAAP.
  - ii. An issuer with a FIFO inventory election.
  - iii. An issuer with a loan covenant that requires the use of U.S. GAAP.
  - iv. An issuer who is included in the S&P 500.
- a. i only.
  - b. i and ii.
  - c. i, iii, and iv.
16. Which of the following companies could expect an easy transition when converting their financial reporting systems to IFRS?
- a. An issuer with relatively simple business transactions.
  - b. An issuer with an extensive geographical reach.
  - c. An issuer with a complex reporting structure.
  - d. An issuer with complex transaction cycles.

17. Which of the following is correct regarding IFRS for SMEs?
- a. IFRS for SMEs is intended to be used by entities that have public accountability.
  - b. A subsidiary of an entity may use IFRS for SMEs as long as it has public accountability.
  - c. An investment in a jointly controlled entity for which there is a published price is measured using the equity method or proportionate consolidation.
  - d. All financial statements of an entity reporting under IFRS for SMEs must comply with the relevant requirements of the standard.
18. The FASB and IASB have two convergence initiatives, the Norwalk Agreement and the Memorandum of Understanding. Did the credit crisis of 2008-2010 have any effect on these documents?
- a. Yes.
  - b. No.
19. The PCFRC has issued several models concerning nonpublic entities that are not required to file financial statements with the SEC. Which of the following choices accurately describes the model known as IFRS with differential reporting?
- a. IFRS would be adopted by all U.S. companies as their accounting framework.
  - b. The framework of IFRS is modified to assist private companies by deleting some requirements.
  - c. U.S. GAAP would be modified into a self-contained accounting framework.
  - d. U.S. private companies would adopt an adapted version of IFRS.
20. Which of the following global networks might the FASB call upon to assist with global needs of the clients of U.S. CPA firms?
- i. The Forum of Firms.
  - ii. The International Federation of Accountants.
  - iii. The Transnational Auditors Committee.
  - iv. The International Auditing and Assurance Standards Board.
- a. i only.
  - b. i and ii.
  - c. i, ii, and iii.
  - d. i, ii, iii, and iv.

## SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

13. Which of the following best describes the overarching reason for the convergence of FASB and IASB standards? **(Page 32)**
  - a. **Investment markets have become global. [This answer is correct. Investors diversify their portfolios by investing globally. Those investors need timely, complete, reliable and comparable financial information thus making a global accounting platform a necessity.]**
  - b. The U.S. share of the worldwide capital markets has fallen to less than half. [This answer is incorrect. While it is true that the U.S. share of market capitalization on the worldwide markets is less than half, this is not the overarching reason for the convergence of FASB and IASB standards.]
  - c. The litigious culture of the U.S. has made it less attractive to companies seeking a stock exchange listing. [This answer is incorrect. Although the U.S. culture may be litigious, the U.S. culture is not the driving force behind the convergence of FASB and IASB standards.]
14. Your client is an investment company regulated under the Investment Company Act of 1940. Is your client included on the IFRS roadmap? **(Page 34)**
  - a. Yes. [This answer is incorrect. The proposed roadmap relates solely to U.S. issuers with respect to their periodic reporting requirements under Sections 13 and 15(d) of the Exchange Act, proxy and information statements under Section 14 of the Exchange Act and registration statements under Section 12 of the Exchange Act and Section 7 of the Securities Act.]
  - b. **No. [This answer is correct. The roadmap does not contemplate adoption of IFRS by investment companies regulated under the Investment Company Act of 1940 (15 USC § 80), or by regulated entities such as registered broker-dealers.]**
15. The IFRS standards are expected to have effects on other reporting requirements. From the list below, select the reporting requirements that will be affected by IFRS. **(Page 37)**
  - i. An issuer required to provide state regulators with a financial statement based on GAAP.
  - ii. An issuer with a FIFO inventory election.
  - iii. An issuer with a loan covenant that requires the use of U.S. GAAP.
  - iv. An issuer who is included in the S&P 500.
  - a. i only. [This answer is incorrect. The transition to IFRS will have an effect on issuers subject to state regulators as well as other issuers.]
  - b. i and ii. [This answer is incorrect. Issuers using the FIFO basis of inventory valuation are not affected by IFRS. IFRS allows FIFO but not the LIFO basis of inventory valuation.]

- c. i, iii, and iv. **[This answer is correct. All of the reporting requirements described in these answer choices will be affected by the IFRS requirements. An issuer required to provide state regulators with GAAP financial statements might have to maintain two sets of records to report under IFRS and GAAP, an issuer may have a contractual obligation such as a loan covenant that requires GAAP reporting, and the S&P 500 currently only includes issuers that file their financial statements using U.S. GAAP.]**
16. Which of the following companies could expect an easy transition when converting their financial reporting systems to IFRS? **(Page 37)**
- a. **An issuer with relatively simple business transactions. [This answer is correct. An issuer with simple business transactions could expect the lead time necessary to convert to IFRS to be less, thus making the transition easier.]**
- b. An issuer with an extensive geographical reach. [This answer is incorrect. An issuer who is spread out geographically will need a longer lead time to design financial reporting systems that are ready for IFRS.]
- c. An issuer with a complex reporting structure. [This answer is incorrect. An issuer with a complex reporting structure can expect to incur more cost and more time in making the transition to IFRS.]
- d. An issuer with complex transaction cycles. [This answer is incorrect. An issuer whose business includes complex transaction cycles can expect to spend more and have a more complex transition to IFRS.]
17. Which of the following is correct regarding IFRS for SMEs? **(Page 41)**
- a. IFRS for SMEs is intended to be used by entities that have public accountability. [This answer is incorrect. IFRS for SMEs is intended for use by entities that do *not* have public accountability and publish general purpose financial statements for external users.]
- b. A subsidiary of an entity may use IFRS for SMEs as long as it has public accountability. [This answer is incorrect. A subsidiary of an entity may use IFRS for SMEs only if it meets the public accountability test.]
- c. An investment in a jointly controlled entity for which there is a published price is measured using the equity method or proportionate consolidation. [This answer is incorrect. Under IFRS for SMEs, this investment would be measured at fair value through profit and loss.]
- d. **All financial statements of an entity reporting under IFRS for SMEs must comply with the relevant requirements of the standard. [This answer is correct. An entity that elects to report under IFRS for SMEs must make an “explicit and unreserved” declaration to that effect in the notes to the financial statements and must comply with all relevant requirements of the standard.]**

18. The FASB and IASB have two convergence initiatives, the Norwalk Agreement and the Memorandum of Understanding. Did the credit crisis of 2008-2010 have any effect on these documents? **(Page 44)**
  - a. **Yes. [This answer is correct. The credit crisis caused both the FASB and IASB to pursue short-term measures to respond to the credit crisis.]**
  - b. No. [This answer is incorrect. Both the FAB and IASB made commitments due to recent economic developments. These economic developments are likely to cause revisions in timetables the Boards had agreed upon to complete various projects.]
19. The PCFRC has issued several models concerning nonpublic entities that are not required to file financial statements with the SEC. Which of the following choices accurately describes the model known as IFRS with differential reporting? **(Page 49)**
  - a. IFRS would be adopted by all U.S. companies as their accounting framework. [This answer is incorrect. The adoption of IFRS by all companies is the model known as IFRS with Private Entities Option.]
  - b. **The framework of IFRS is modified to assist private companies by deleting some requirements. [This answer is correct. Some requirements would be deleted or different treatments would be embedded in the standards to meet the unique needs of U.S. private companies. This accurately describes the model known as IFRS with Differential Reporting.]**
  - c. U.S. GAAP would be modified into a self-contained accounting framework. [This answer is incorrect. Building current U.S. GAAP into a comprehensive, self-contained accounting standards framework suitable for private companies is the model known as Separate U.S. Private Company GAAP Adapted from Current U.S. GAAP.]
  - d. U.S. private companies would adopt an adapted version of IFRS. [This answer is incorrect. The model under which U.S. private companies adopt an adapted version of IFRS is the model known as U.S. Adapted Version of IFRS for SMEs.]
20. Which of the following global networks might the FASB call upon to assist with global needs of the clients of U.S. CPA firms? **(Page 49)**
  - i. The Forum of Firms.
  - ii. The International Federation of Accountants.
  - iii. The Transnational Auditors Committee.
  - iv. The International Auditing and Assurance Standards Board.
  - a. i only. [This answer is incorrect. The Forum of Firms (FOF) is not the only global network with the potential to assist the FASB across national borders.]
  - b. i and ii. [This answer is incorrect. In addition to the FOF, the International Federation of Accountants (IFAC) is not the only global network that may assist the FASB in the area of audit and other assurance related topics.]
  - c. **i, ii, and iii. [This answer is correct. The FOF, IFAC and the Transnational Auditors Committee (TAC) all have the potential to be global networks able to assist the FASB with the global needs of clients.]**
  - d. i, ii, iii, and iv. [This answer is incorrect. To be a member of the FOF, one of the requirements is that the member maintain appropriate quality control standards issued by the International Auditing and Assurance Standards Board (IAASB). However, the IAASB is not a network of accounting firms that the FASB would call upon.]





## EXAMINATION FOR CPE CREDIT

### Lesson 2

Determine the best answer for each question below. Then log onto our Online Grading Center at **OnlineGrading.Thomson.com** to record your answers.

12. When did the SEC first express a desire to standardize the U.S. GAAP and international disclosure standards?
  - a. 1979.
  - b. 1988.
  - c. 2002.
  - d. 2007.
13. Mary L. Schapiro, Chairman of the SEC gave testimony before the Senate Committee on Banking, Housing, and Urban Affairs about the IFRS Roadmap. Which of the following was her position on adoption of the Roadmap?
  - a. She believes that the Roadmap should be fully adopted and implemented as scheduled.
  - b. She believes that the U.S. should proceed with great caution and not rush into implementing the roadmap.
  - c. She believes that the cost to implement the IFRS Roadmap switching from GAAP to IFRS should be minimal for most corporations.
  - d. She believes that the U.S. should be responsible for establishing international financial reporting standards, and therefore we should not adopt the Roadmap.
14. The IFRS Roadmap uses a milestone-based approach. Which of the following is **not** one of the milestones?
  - a. Education and training.
  - b. Improvements to IFRS.
  - c. Revision of the Internal Revenue Code to eliminate IFRS issues.
  - d. Accountability and funding of the IASC Foundation.
15. If a company wants to file an IPO and has previously been reporting under U.S. GAAP, which of the following would require substantial costs to be incurred before the IPO could be filed with the SEC?
  - a. Paying filing fees for the registration.
  - b. Printing and distributing information related to the public offering.
  - c. Travel costs to meet with the SEC staff for multiple reviews of the offering document.
  - d. Providing IFRS compliant audited financial statements for the initial registration filing.

16. Before adopting IFRS, the SEC is considering several things related to IFRS. Which of the following is one of those items?
- a. The rules-based guidance and safe harbors provided by IFRS.
  - b. The substantial guidance in IFRS for the extractive industries.
  - c. Whether IFRS is being consistently applied across companies and across industries.
  - d. The significant amount of detailed implementation guidance provided by IFRS.
17. Regarding IFRS, which of the following is correct?
- a. IFRS provides adequate guidance on reorganizations.
  - b. Safe harbors do not apply to information appearing in the notes to audited financial statements.
  - c. IFRS does not require disclosure in the notes to the financial statements of sensitivity analyses.
  - d. IFRS has worldwide uniform adoption of its standards.
18. Which of the following has been accounted for correctly under IFRS for SMEs?
- a. Investment property whose fair value can be reliably measured without undue cost or effort measured by cost-depreciation-impairment model.
  - b. Investment in an associate for which there is a published price measured using the equity method.
  - c. Unvested past service cost recognized immediately in profit or loss. (Page 39)
  - d. Noncurrent assets held-for-sale measured at lower of carrying amount and fair value less costs to sell.
19. The Norwalk Agreement resulted in the issuance of a Memorandum of Understanding between the FASB and the IASB. This memorandum was based on three overriding principles. Which of the following is **not** one of those principles?
- a. Issue common standards that improve information provided to investors.
  - b. Convergence of accounting standards is best achieved through development of high-quality common standards.
  - c. Both boards should seek convergence by replacing standards in need of improvement with jointly developed new standards.
  - d. FASB would eventually become the only recognized globally accepted standard setter.
20. Which of the following statements is correct concerning IFRS support in the U.S.?
- a. The Uniform CPA Exam now includes IFRS on its list of study materials for the Financial Accounting and Reporting part of the exam.
  - b. The AICPA council passed a resolution in 2008 designating the SEC as the body to establish international financial accounting and reporting standards.
  - c. The AICPA Board of Examiners for the Uniform CPA Exam has stated that exams beginning in 2009 will include questions on IFRS.
  - d. The AICPA council passed a resolution in 2008 designating the IASB as the body to establish accounting standards for the U.S.

## Glossary

**A&A Guides** – AICPA Accounting and Auditing Guides.

**AcSEC** – AICPA Accounting Standards Executive Committee.

**AIA** – American Institute of Accountants. The IPA changed its name to the AIA in 1917. In 1957, the AIA changed its name to the AICPA.

**AICPA** – American Institute of Certified Public Accountants.

**APB** – Accounting Principles Board.

**ARB** – Accounting Research Bulletins.

**ASC** – Accounting Standards Codification.

**ASCPA** – American Society of Certified Public Accountants. This was a federation of state CPA societies formed in 1921. The ASCPA merged into the AIA in 1936.

**EITF** – FASB Emerging Issues Task Force.

**FASAB** – Federal Accounting Standards Advisory Board.

**FASB** – The Financial Accounting Standards Board (FASB) is an independent authoritative body created in 1973 to replace the American Institute of Certified Public Accountants (AICPA) Accounting Principles Board and authorized by the AICPA *Code of Professional Conduct* as a promulgator of generally accepted accounting principles (GAAP), primarily for nongovernment entities.

**FASB Cleared** – FASB reviewed and sanctioned authoritative guidance.

**GASB** – The Government Accounting Standards Board (GASB) is the body authorized to promulgate standards of financial accounting and reporting for state and local governmental units. It was created by the Financial Accounting Foundation (FAF) in 1984 as successor to the National Council on Governmental Accounting (NCGA) and is recognized by the *Code of Professional Conduct* as an authorized body whose pronouncements must be followed in order to conform to Rules 202 and 203.

**IASB** – The International Accounting Standards Board (IASB) is an independent, private sector standards-setting body founded in 1973 by professional accounting organizations in nine countries. The IASB issues International Financial Reporting Standards.

**IASC** – The International Accounting Standards Committee (IASC) is an independent private sector body with the objective of achieving uniformity in the accounting principles used around the world. The IASC issues Statements of International Accounting Standards. However, these Standards do not establish standards enforceable under the Code of Professional Conduct of the AICPA. The IASC was formed in 1973 through an agreement made by professional accounting bodies from 10 countries, including the United States.

**OCBOA** – Other Comprehensive Basis of Accounting. Financial records are maintained and reported according to a basis other than GAAP. A comprehensive basis of accounting other than GAAP is one of the following:

- A basis of accounting that the entity used to comply with the requirements or financial reporting provisions of a governmental regulatory agency to whose jurisdiction the entity is subject (e.g., pursuant to the rules of a state insurance commission).
- A basis of accounting used to file income tax returns for the period covered by the financial statements.
- The cash receipts and disbursements basis of accounting, and modifications of the cash basis when such modifications are substantially supported, such as recording depreciation on fixed assets or accruing income taxes.
- A definite set of criteria having substantial support that is applied to all items appearing in financial statements, such as the price level basis of accounting.

**PCAOB** – The Public Company Accounting Oversight Board (PCAOB) was founded under the provisions of Title I of the Sarbanes-Oxley Act of 2002. The language in Title I that establishes the board and sets its status parallels the structure of the Federal Deposit Insurance Corporation (FDIC), which insures bank deposits and regulates a significant portion of the banking industry.

The act sets the following criteria for the PCAOB:

- a. Establishment of Board—There is established the Public Company Accounting Oversight Board, to oversee the audit of public companies that are subject to the securities laws, and related matters, in order to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports for companies the securities of which are sold to, and held by and for, public investors. The Board shall be a body corporate, operate as a nonprofit corporation, and have succession until dissolved by an Act of Congress.
- b. Status—The Board shall not be an agency or establishment of the United States Government, and, except as otherwise provided in this Act, shall be subject to, and have all the powers conferred upon a nonprofit corporation by, the District of Columbia Nonprofit Corporation Act. No member or person employed by, or agent for, the Board shall be deemed to be an officer or employee of or agent for the Federal Government by reason of such service.

**POB** – Public Oversight Board, a precursor to the PCAOB.

**Q&As** – AICPA accounting interpretations and implementation guides, published by FASB staff.

**SEC** – The Securities and Exchange Commission (SEC) is a federal government agency charged with the responsibility of writing rules consistent with federal security laws, investigation of violations, maintenance of financial disclosure documentation, and the initiation of action against violators of federal securities acts. The SEC's main office is in Washington, D.C., but it has “enforcement” and field offices throughout the country.

The SEC is charged with the oversight of the Federal Securities Act of 1933, the Federal Securities Exchange Act of 1934, and the Foreign Corrupt Practices Act. The agency serves to govern the registration, offering, sale, and so forth of stocks, bonds, notes, convertible debentures, warrants, or other financial documents involving investments and purchases.

In addition to writing regulations, the SEC reviews registration statements for compliance with disclosure requirements. The SEC does not determine whether the information provided to investors is accurate or truthful, nor does the SEC determine whether the terms of the offering are fair or reasonable to investors.

The mission of the SEC is to protect the integrity of capital markets through enforcement of financial disclosure laws that apply when a business entity attempts to raise capital by selling ownership to investors. The SEC defines what information prospective investors must receive from offerors and what information the entities must continue to report to their shareholders if the entity has a certain number of owners.

**SFAC** – FASB Statements of Financial Accounting Concepts.

**SFAS** – FASB Statements of Financial Accounting Standards.

**SOP** – AICPA Statements of Position.

**SOX** – After major financial fraud brought down companies such as WorldCom and Enron, the U.S. Congress passed the Sarbanes-Oxley Act of 2002 (SOX). The act's major provisions relating to auditors of public companies can be explained as follows:

- The act establishes the Public Company Accounting Oversight Board (PCAOB). The board has the authority to regulate public accounting firms, including setting audit rules and ethics guidelines. All accounting firms that audit public companies must register with the PCAOB and the board must inspect them regularly.
- The independent auditors must communicate regularly and completely with the audit committee of their audit clients.
- In order to avoid conflicts of interest, the act establishes a rule that an accounting firm cannot audit a company if one of the company's top officers worked for the accounting firm in the last year and was involved in the company's audit.
- The act establishes term limits so that a lead audit partner cannot work on a client's audit in any auditing role for more than five years.
- The act ordered a study of the factors that since 1989 have caused the Big Eight accounting firms to shrink to the Big Four (Deloitte & Touche, Ernst & Young, KPMG, and PricewaterhouseCoopers).

The Sarbanes-Oxley Act of 2002 applies to publicly held companies and other issuers. It is intended to provide the investing public with greater assurance about the reliability of a public company's financial reporting in quarterly and annual filings with the SEC.

Section 404 of SOX requires that public companies have an audit of their internal controls in conjunction with the audit of their financial statements. The audit is to be conducted in accordance with Auditing Standard No. 2, issued by the PCAOB. Visit the PCAOB website for additional information.

There is a push by some states and regulators to extend the provisions of SOX to nonpublic companies and not-for-profit entities and their auditors.

**XBRL** – eXtensible Business Reporting Language.

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# Testing Instructions for Examination for CPE Credit

## Decoding the FASB Codification (CODTG10)

1. Following these instructions is information regarding the location of the **CPE Credit Examination Questions**.
2. Log on to our Online Grading Center at **Online Grading.Thomson.com** to receive instant CPE credit. Click the purchase link and a list of exams will appear. Search for the exam by selecting PPC in the drop-down box under Brand. Payment of \$49 for the exam is accepted over a secure site using your credit card. Once you purchase an exam, you may take the exam three times. On the third unsuccessful attempt, the system will request another payment. Once you successfully score 70% on an exam, you may print your completion certificate from the site. The site will retain your exam completion history. If you lose your certificate, you may return to the site and reprint your certificate.
3. To receive CPE credit, the online exam must be completed by **August 31, 2011**. CPE credit will be given for examination scores of 70% or higher.
4. Please direct any questions or comments to our Customer Service department at (800) 323-8724

## EXAMINATION FOR CPE CREDIT

To enhance your learning experience, examination questions are located immediately following each lesson. Each set of examination questions can be located on the page numbers listed below. The course is designed so the participant reads the course materials, answers a series of self-study questions, and evaluates progress by comparing answers to both the correct and incorrect answers and the reasons for each. At the end of each lesson, the participant then answers the examination questions and records answers to the examination questions on either the printed **Examination for CPE Credit Answer Sheet** or by logging on to the **Online Grading System**. The **Examination for CPE Credit Answer Sheet** and **Self-study Course Evaluation Form** are located at the end of the course materials. For more information on completing the **Examination for CPE Credit**, see the **Testing Instructions** on the preceding page.

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