



July 2013

# A&A Update

The Technical Standards Update of Crowe Horwath International

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## From the Standards Setters

### **FASB Issues ASU No. 2013-8 to Set U.S. GAAP Criteria for Investment Companies**

ASU No. 2013-08, *Financial Services—Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements*, was issued on June 7, 2013. It establishes new criteria for determining when a business should be considered an investment company for accounting purposes. The update makes extensive changes to Topic 946, Financial Services—Investment Companies, formerly the AICPA's Audit and Accounting Guide, *Investment Companies*, and Statement of Position (SOP) No. 07-1.

The changes are effective for fiscal years starting after December 15, 2013. Businesses that are no longer considered investment companies because of the amendments to Topic 946 will have to stop applying the topic and report the change in status as an adjustment to retained earnings.

Businesses that are redefined as investment companies because of the changes in ASU No. 2013-08 should adjust their net assets at the start of the next fiscal year or quarter to reflect the new status, but won't have to restate old financial statements.

In October 2012, the IASB issued *Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27)*. While the approaches to the investment company assessment are similar, the scope of investment company guidance under IFRS is narrower because it provides only an exception to consolidation guidance. The guidance under IFRS requires a controlled investee to be present for a company to be eligible for the investment entity exception to consolidation guidance. In contrast, longstanding US GAAP has provided comprehensive accounting and reporting guidance for investment companies.

### **Three Proposals Will Address GAAP Amendments for Private Companies**

In June, the FASB agreed to release three proposals put forth by its Private Company Council (PCC) to simplify some accounting practices for private companies.

The three proposals (a) scale back accounting requirements for intangible assets acquired during business combinations, (b) allow an acquirer's amortization of goodwill following a merger, and (c) simplify the accounting for some common interest rate swaps.

When released, the proposals will be out for two-month comment periods.

PCC Issue No. 13-01A, *Accounting for Identifiable Intangible Assets in a Business Combination*, would allow private companies to skip recognizing some types of intangible assets acquired when they buy or merge with another business. The PCC proposal would narrow the type of intangible assets private

companies would have to recognize and measure at fair value to those linked to contracts or legal obligations. Intangible assets with hard-to-determine values, such as customer lists or unpatented technology, would not have to be measured.

PCC Issue No. 13-01B, *Accounting for Goodwill Subsequent to a Business Combination*, would allow companies the option to amortize goodwill over a maximum 10-year period. A private company only would have to test goodwill for impairment when it determines that it is "more likely than not" that the company's fair value is below its carrying amount.

PCC Issue No. 12-03, *Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps*, offers private companies a simpler approach to accounting for "plain vanilla" interest rate swaps. Businesses would be allowed two options to account for the swaps. (1) The swap and the loan could be accounted for as one instrument. The swap would stay off the company's balance sheet, but its termination value would be disclosed in the financial statement footnotes. (2) A company also could choose to record the swap at termination value, as opposed to fair value, on the balance sheet. Privately-held banks and other private financial institutions, however, would not be allowed to use this break.

### **FASB Votes to Allow Private Companies an Indefinite Deferral on Value in Employee Stock Plans**

In June, the FASB voted unanimously to allow private companies an indefinite deferral from disclosing the value of company stock held by employee stock ownership plans, despite a warning from the Department of Labor that the disclosures were "critical" for regulators and plan beneficiaries. The deferral will be effective as soon as the FASB publishes the update.

### **Updated COSO Framework – How the Changes May Impact Clients**

Here are a few areas in which clients will need to pay close attention to insure that their existing controls framework meets the requirements of the new COSO framework:

- Outsourcing - Clients can outsource activity, but the client retains responsibility for the outsourced activity.
- Fraud - The control structure must address fraud issues directly.
- Information Technology (IT) – IT is a critical component of today's environment that cannot be avoided. The controls over IT operations must be an integral part of the control system.

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## **Headlines from Around the World**

### **FRC Issues Revised Auditing Standard: Making Auditors' Work More Transparent to Investors**

In June, the FRC made a significant change to the UK's corporate governance regime with the issue of its revised auditing standard enhancing the transparency of the auditor's report with the aim of better communication to investors. The revisions to ISA 700 (UK and Ireland) "*The Independent Auditor's Report on Financial statements*" require auditors reporting on companies which apply the UK Corporate Governance Code to explain more about their work.

Under the revised standard, auditors are to:

- Provide an overview of the scope of the audit, showing how this addressed the risk and materiality considerations
- Describe the risks that had the greatest effect on:

- the overall audit strategy
- the allocation of resources in the audit
- directing the efforts of the engagement team
- Provide an explanation of how they applied the concept of materiality in planning and performing the audit

The revised standard is designed to complement changes made to the UK Corporate Governance Code in October 2012. Accordingly it is effective for audits of financial statements for periods commencing on or after 1 October 2012.

### **AICPA Releases Non-GAAP Reporting Framework**

The AICPA has released its [Financial Reporting Framework for Small- and Medium-Sized Entities](#) (FRF for SME), which is aimed at providing an alternative reporting option for small businesses that **aren't required to use GAAP**. It is worth repeating that this FRF **is not GAAP** and entities considering its use will need to be sure that it will meet its financial statement users' needs. It is also important to note that the use of this FRF is completely voluntary as the AICPA has absolutely no authority to mandate its use. As its use is voluntary, there is no effective date, i.e. it may be used immediately.

The new framework uses only historical cost as a basis for valuing assets and liabilities, not current market value. It doesn't include more-complex accounting for areas that smaller, simpler companies are unlikely to get into, such as off-balance-sheet entities, derivatives or hedging.

### **IFRS Foundation Sets Out Country Progress on IFRS**

The IFRS Foundation has completed the first phase of an initiative which charts how far different jurisdictions have progressed towards global adoption of International Financial Reporting Standards (IFRS). In the first stage of the work to assess worldwide progress on adoption, the standards body has published IFRS profiles for all G20 jurisdictions, as well as profiles for a further 46 jurisdictions who responded to a survey of national and regional bodies with overall responsibility for accounting standards within their jurisdiction.

Of the 66 jurisdictions surveyed, 95% have made public commitments supporting IFRS as the single set of financial reporting standards suitable for global application. The majority (80%) have already adopted IFRS as a requirement for all or nearly all companies whose securities are publicly traded, with the remainder well on the way to doing so.

The survey also shows that those jurisdictions who have adopted IFRS have done so with very few modifications. Most changes are regarded as being temporary, and are associated with standards where IASB is already working on updates. Over half of jurisdictions have either already adopted the IFRS for SMEs or are planning to do so in the near future.

Michel Prada, chairman of the IFRS Foundation trustees, said: 'Although different countries are at different stages along the path to IFRS adoption, the direction of travel is clear and the momentum is unstoppable.'

A second phase of the project is under way with the goal of providing profiles for most jurisdictions by the end of 2013.

The country profiles are available [here](#).

### **NASBA Tells Private Companies: Don't Use AICPA Financial Reporting Framework**

The National Association of State Boards of Accountancy (NASBA) has advised private companies not to use the American Institute of CPAs' recently released Financial Reporting Framework for Small and Medium-sized Entities. NASBA reaffirmed its support of GAAP as modified by FASB to meet the financial reporting needs of private companies.

NASBA noted that it is the national organization for the 55 U.S. Boards of Accountancy which have a Constitutional responsibility to protect the public, including ensuring that high quality standards are upheld by CPAs and their firms. Forty years ago, both the SEC and the AICPA agreed that FASB would be the single, duly-authorized body to promulgate accounting standards.

In the interest of furthering public protection, NASBA is developing recommended rule language prohibiting the use of non-authoritative standards unless it is acceptable to Boards of Accountancy.

### **FRC Prohibits the Use of Internal Audit Staff on the External Audit Team**

The UK's Financial Reporting Council has introduced a measure that creates a clearer division of responsibility between internal and external audit teams to safeguard against conflicts of interest. By prohibiting auditors from using internal audit staff as "direct assistance" members of the audit team, the FRC is seeking to ensure the independence of the external auditor and promote greater confidence in the integrity of the audit for investors. This will create a difference in standards for the UK as both ISA and AU 610 allow "direct assistance" under certain circumstances. Editor's note – The FRC has it right.

### **UK Pension Fund Group Says Accounting Rules Clash with Law**

IFRS follow an incurred-loss model, which allow banks to wait until financial assets are close to default before realizing a loss. According to the London-based **Local Authority Pension Fund Forum** (LAPFF) this contradicts UK law which calls for "a true and fair" view of profit. Accounting rules are also a matter of law in the European Union as the EU actually legislates approval of IFRS. Perhaps the LAPFF would prefer in this instance US GAAP which follows an expected-loss model. It will be interesting to see how this plays out in the UK.

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## **Useful Links**

- International Accounting Standards Board (IASB) [www.iasb.org](http://www.iasb.org)
- [IASB Exposure Drafts open for comment](#)
- International Auditing and Assurance Standards Board (IAASB) [www.ifac.org/iaasb](http://www.ifac.org/iaasb)
- International Federation of Accountants (IFAC) [www.ifac.org](http://www.ifac.org)
- [IFRS Interpretations Committee \(IFRIC\)](#)
- Financial Accounting Standards Board (FASB) [www.fasb.org](http://www.fasb.org)
- Public Company Accounting Oversight Board (PCAOB) [www.pcaob.org](http://www.pcaob.org)
- [American Institute of CPAs Auditing Standards Board \(AICPA ASB\)](#)
- United States Securities and Exchange Commission (SEC) [www.sec.gov](http://www.sec.gov)
- European Commission (EC)
- [Forum of Firms \(FoF\)](#)
- [Transnational Auditors Committee \(TAC\)](#)
- [TAC Guidance Statement No. 1, Definition of Transnational Audit](#)
- UK Financial Reporting Council [www.frc.org.uk](http://www.frc.org.uk)
- [AICPA Center for Audit Quality document explaining PCAOB inspections](#)

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Editor-in-Chief: Howard Sibelman  
Editors: David Chitty, Beth Share

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