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Financial Accounting Standards Board (FASB)

Summary of Activities

July 1973 – March 1980
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Financial Accounting Standards Board (FASB)

Summary of Activities

July 1973 — March 1980
## TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction</td>
<td>1</td>
</tr>
<tr>
<td>Background</td>
<td>1</td>
</tr>
<tr>
<td>Members</td>
<td>1</td>
</tr>
<tr>
<td>Procedures</td>
<td>2</td>
</tr>
<tr>
<td>Statements</td>
<td></td>
</tr>
<tr>
<td>Interpretations</td>
<td></td>
</tr>
<tr>
<td>Technical Bulletins</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td></td>
</tr>
<tr>
<td><strong>Recent Developments</strong></td>
<td>2</td>
</tr>
<tr>
<td><strong>Statements of Financial Accounting Concepts Issued</strong></td>
<td>4</td>
</tr>
<tr>
<td>Purpose and Authority</td>
<td></td>
</tr>
<tr>
<td>No. 1 — <em>Objectives of Financial Reporting by Business Enterprises</em> (November 1978)</td>
<td></td>
</tr>
<tr>
<td><strong>Statements of Financial Accounting Standards Issued</strong></td>
<td>7</td>
</tr>
<tr>
<td>No. 1 — <em>Disclosure of Foreign Currency Translation Information</em> (December 1973) (Superseded by FASB Statement No. 8, October 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 2 — <em>Accounting for Research and Development Costs</em> (October 1974)</td>
<td></td>
</tr>
<tr>
<td>No. 3 — <em>Reporting Accounting Changes in Interim Financial Statements</em> (December 1974)</td>
<td></td>
</tr>
<tr>
<td>No. 4 — <em>Reporting Gains and Losses from Extinguishment of Debt</em> (March 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 5 — <em>Accounting for Contingencies</em> (March 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 6 — <em>Classification of Short-Term Obligations Expected To Be Refinanced</em> (May 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 7 — <em>Accounting and Reporting by Development Stage Enterprises</em> (June 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 8 — <em>Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements</em> (October 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 9 — <em>Accounting for Income Taxes — Oil and Gas Producing Companies</em> (October 1975) (Superseded by FASB Statement No. 19, December 1977)</td>
<td></td>
</tr>
<tr>
<td>No. 10 — <em>Extension of “Grandfather” Provisions for Business Combinations</em> (October 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 11 — <em>Accounting for Contingencies — Transition Method</em> (December 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 12 — <em>Accounting for Certain Marketable Securities</em> (October 1975)</td>
<td></td>
</tr>
<tr>
<td>No. 13 — <em>Accounting for Leases</em> (November 1976)</td>
<td></td>
</tr>
</tbody>
</table>
No. 15 — Accounting by Debtors and Creditors for Troubled Debt Restructurings (June 1977)

No. 16 — Prior Period Adjustments (June 1977)

No. 17 — Accounting for Leases — Initial Direct Costs (November 1977)

No. 18 — Financial Reporting for Segments of a Business Enterprise — Interim Financial Statements (November 1977)

No. 19 — Financial Accounting and Reporting by Oil and Gas Producing Companies (December 1977)

No. 20 — Accounting for Forward Exchange Contracts (December 1977)

No. 21 — Suspension of the Reporting of Earnings Per Share and Segment Information by Nonpublic Enterprises (April 1978)

No. 22 — Changes in the Provisions of Lease Agreements Resulting From Refundings of Tax-Exempt Debt (June 1978)

No. 23 — Inception of the Lease (August 1978)

No. 24 — Reporting Segment Information in Financial Statements That Are Presented In Another Enterprise’s Financial Report (December 1978)

No. 25 — Suspension of Certain Accounting Requirements for Oil and Gas Producing Companies (February 1979)

No. 26 — Profit Recognition on Sales-Type Leases of Real Estate (April 1979)

No. 27 — Classification of Renewals or Extensions of Existing Sales-Type or Direct Financing Leases (May 1979)

No. 28 — Accounting for Sales With Leasebacks (May 1979)

No. 29 — Determining Contingent Rentals (June 1979)

No. 30 — Disclosure of Information About Major Customers (August 1979)

No. 31 — Accounting for Tax Benefits Related to U.K. Tax Legislation Concerning Stock Relief (September 1979)

No. 32 — Specialized Accounting and Reporting Principles and Practices in AICPA Statements of Position and Guides on Accounting and Auditing Matters (September 1979)

No. 33 — Financial Reporting and Changing Prices (September 1979)

No. 34 — Capitalization of Interest Cost (October 1979)

No. 35 — Accounting and Reporting by Defined Benefit Pension Plans (March 1980)

Interpretations Issued

No. 1 — Accounting Changes Related to the Cost of Inventory (June 1974)

No. 2 — Imputing Interest on Debt Arrangements Made Under the Federal Bankruptcy Act (June 1974) (Superseded by FASB Statement No. 15, June 1977)

No. 3 — Accounting for the Cost of Pension Plans Subject to the Employee Retirement Income Security Act of 1974 (December 1974)

No. 4 — Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method (February 1975)
No. 5 — *Applicability of FASB Statement No. 2 to Development Stage Enterprises* (February 1975) (Superseded by FASB Statement No. 7, June 1975)

No. 6 — *Applicability of FASB Statement No. 2 to Computer Software* (February 1975)

No. 7 — *Applying FASB Statement No. 7 in Financial Statements of Established Operating Enterprises* (October 1975)

No. 8 — *Classification of a Short-Term Obligation Repaid Prior to Being Replaced by a Long Term Security* (January 1976)

No. 9 — *Applying APB Opinions No. 16 and 17 When a Savings and Loan Association or a Similar Institution Is Acquired in a Business Combination Accounted for by the Purchase Method* (February 1978)

No. 10 — *Application of FASB Statement No. 12 to Personal Financial Statements* (September 1976)

No. 11 — *Changes in Market Value After the Balance Sheet Date* (September 1976)

No. 12 — *Accounting for Previously Established Allowance Accounts* (September 1976)

No. 13 — *Consolidation of a Parent and Its Subsidiaries Having Different Balance Sheet Dates* (September 1976)


No. 15 — *Translation of Unamortized Policy Acquisition Costs by a Stock Life Insurance Company* (September 1976)

No. 16 — *Clarification of Definitions and Accounting for Marketable Equity Securities That Become Nonmarketable* (February 1977)

No. 17 — *Applying the Lower of Cost or Market Rule in Translated Financial Statements* (February 1977)

No. 18 — *Accounting for Income Taxes in Interim Periods* (March 1977)

No. 19 — *Lessee Guarantee of the Residual Value of Leased Property* (October 1977)

No. 20 — *Reporting Accounting Changes Under AICPA Statements of Position* (November 1977)

No. 21 — *Accounting for Leases in a Business Combination* (April 1978)

No. 22 — *Applicability of Indefinite Reversal Criteria to Timing Differences* (April 1978)

No. 23 — *Leases of Certain Property Owned by a Governmental Unit or Authority* (August 1978)

No. 24 — *Leases Involving Only Part of a Building* (September 1978)

No. 25 — *Accounting for an Unused Investment Tax Credit* (September 1978)

No. 26 — *Accounting for Purchase of a Leased Asset by the Lessee During the Term of the Lease* (September 1978)

No. 27 — *Accounting for a Loss on a Sublease* (November 1978)

No. 28 — *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans* (December 1978)
No. 29 — Reporting Tax Benefits Realized on Disposition of Investments in Certain Subsidiaries and Other Investees (February 1979)

No. 30 — Accounting for Involuntary Conversions of Nonmonetary Assets to Monetary Assets (September 1979)

No. 31 — Treatment of Stock Compensation Plans in EPS Computations (February 1980)

No. 32 — Application of Percentage Limitations in Recognizing Investment Tax Credit (March 1980)

Technical Bulletins Issued

Exposure Drafts Issued and Outstanding

Proposed Statements of Concepts

Qualitative Characteristics: Criteria for Selecting and Evaluating Financial Accounting and Reporting Policies (August 9, 1979)


Objectives of Financial Reporting by Nonbusiness Organizations (March 14, 1980)

Proposed Statements of Standards

Lessee's Use of Interest Rate Implicit in the Lease, an amendment of FASB Statement No. 13 (November 6, 1978) (Withdrawn December 12, 1979)

Estimates of Residual Values by Lessors and Lessees, an amendment of FASB Statement No. 13 (May 10, 1979) (Withdrawn December 12, 1979)

Interim Special Industry Reports on FASB Statement No. 33, Financial Reporting and Changing Prices (May 31, 1979 and June 12, 1979)

Disclosure of Pension and Other Post-Retirement Benefit Information, an amendment of APB Opinion No. 8 (July 12, 1979)

Accounting for Compensated Absences (December 17, 1979)

Accounting for Preacquisition Contingencies of Purchased Enterprises, an amendment of APB Opinion No. 16 (December 26, 1979)

Balance Sheet Classification of Deferred Income Taxes, an amendment of APB Opinion No. 11 (March 1980)

Proposed Interpretations

Reporting Intercorporate Income Tax Allocations, an interpretation of APB Opinions No. 11 and 22 (August 20, 1979) (Remanded to AcSEC for specific problems situations.)

Applicability of APB Opinion No. 21 to Television Film License Agreements, an interpretation of APB Opinion No. 21 (September 28, 1979)

Applying FASB Statement No. 34 to Oil and Gas Producing Operations Accounted by the Full Cost Method, an interpretation of FASB Statement No. 34 (January 28, 1980)
Discussion Memoranda Issued (for which Exposure Drafts have not been issued to date)  60

Concepts


  *Criteria for Determining Materiality* (Issued March 1975) (The project has been combined with the Qualitative Characteristics project)

  *Reporting Earnings* (Issued July 31, 1979)

Standards

  *Accounting for Research and Development and Similar Costs* (Issued December 28, 1973)

  *Accounting for Business Combinations and Purchased Intangibles* (Issued August 19, 1976)

  *Interim Financial Accounting and Reporting* (Issued May 25, 1978)

  *Effect of Rate Regulation on Accounting for Regulated Enterprises* (Issued December 31, 1979)

Invitations to Comment  65

  *Evaluation of FASB Statements in Effect at Least Two Years* (Issued May 31, 1978)

Research Reports Issued  66

  *Field Tests of Financial Reporting in Units of General Purchasing Power* (May 1977)


  *Economic Consequences of Financial Accounting Standards — Selected Papers* (July 1978)


Proceedings Issued  69

  *Financial Reporting and Changing Prices — The Conference*, Paul A. Griffin, Editor (June 1979)
Background Papers Issued
*Accounting for Pensions by Employers* (March 1980)

Technical Agenda Projects (for which Discussion Memoranda or Exposure Drafts have not been issued to date) 69

Staff Agenda Projects (not on FASB technical agenda at this date but under study by the Staff) 70

Interpretations and Amendments in Process (for which Discussion Memoranda or Exposure Drafts have not been issued) 70

Research Reports in Process 70

Other Matters (items proposed to the FASB by various parties but not yet placed on the FASB's technical agenda) 71
INTRODUCTION

This booklet provides a ready general reference to the activities of the Financial Accounting Standards Board (FASB). It gives a brief description of the FASB, the procedures followed in issuing its pronouncements, and a synopsis of the provisions of the individual Statements, Interpretations, Discussion Memoranda, Exposure Drafts, Technical Bulletins, and Research Reports issued and proposed to date. The booklet concludes with a listing representing those topics under consideration by the Board as of March 1980.

The booklet should be useful as a general reference; however, the specific pronouncements should be used if a more thorough understanding is needed.

BACKGROUND

In March 1971, the Wheat Committee was established by the American Institute of Certified Public Accountants (AICPA) to study methods for formulation of accounting principles. In March 1972 the Wheat Committee proposed establishment of the Financial Accounting Foundation (FAF), the Financial Accounting Standards Board (FASB) and its related Financial Accounting Standards Advisory Council (FASAC). Later that year, Council of the AICPA endorsed the Wheat Committee report and designated the FASB as the body responsible for formulating accounting standards enforceable by Section 203 of the AICPA Rules of Conduct of the Code of Professional Ethics. AICPA Council also named the FASB as the body to maintain prior APB Opinions, ARB Bulletins, and AICPA Interpretations.

The FAF was established in June 1972. Ralph Kent, chairman and eight other trustees were appointed in July 1972. The Foundation’s trustees included representatives from five constituent groups including the Financial Executives Institute, The National Association of Accountants, the American Accounting Association, and the Financial Analysts Federation, in addition to the AICPA. Marshall Armstrong was named as the first chairman of the FASB in November; by July 1973 all seven members were in place. The first FASB Statement was issued in December 1973. The APB meanwhile completed its final term on June 30, 1973. In 1979, the Board agreed to assume responsibility for AICPA Industry Audit and Accounting Guides and AICPA Statements of Position (SOP). Also in 1979, the FASB was named by the AICPA as the body designated to issue pronouncements regarding supplementary information under Rule 204 of the AICPA Rules of Conduct of the Code of Professional Ethics.

MEMBERS

The present FASB consists of the following persons:

— Chairman Donald J. Kirk, formerly a partner of Price Waterhouse & Co. His term expires December 1981.


— Frank E. Block, formerly a vice-president of Bache Halsey Stuart. His term expires December 1980.


— L. David Mosso, formerly Assistant Secretary of the Treasury. His term expires December 1982.

— Ralph E. Walters, formerly a partner of Touche Ross & Co. His term expires December 1983.
PROCEDURES

Statements

The FASB issues various types of pronouncements. Two, Statements of Financial Accounting Standards and Statements of Financial Accounting Concepts, follow the same procedural process. The FASB consults with FASAC and the Emerging Problems Steering Committee (EPSC) to identify problems, set agenda priorities and appoint task forces to work on problems. On any particular agenda item, a task force defines the problem, does research and prepares a Discussion Memorandum. The Discussion Memorandum is widely distributed and responses are solicited. Once received, these responses become part of the public record. After responses are received, a public hearing is held, usually within 60 days, although at the discretion of the Board, the public hearing may be waived. After the public hearing, an Exposure Draft of a proposed Statement is prepared and issued for public comment. The exposure period is usually 60 days although it may be shorter or longer as necessary. After comments on the Exposure Draft are received and analyzed, modifications, if any, are made and a ballot draft is issued to the Board for written approval. If approved by at least a simple majority (but not less than three) of the members of the Board, the Statement is issued.

Interpretations

Interpretations are usually initiated by a request for clarification from outside parties. The Board generally consults with EPSC to determine the extent and criticalness of the specified situation. A proposed Interpretation is then issued for comment; although exposure to FASAC for a minimum of 15 days is required, proposed Interpretations are generally exposed to the public for a minimum of 30 days.

Technical Bulletins

Technical Bulletins (TB) provide guidance concerning the application of official pronouncements. These Bulletins are not official pronouncements to which Rule 203 applies. Accordingly, the full due-process procedures of the FASB are not applicable. They are issued by the Staff of the Board, but individual Board members are informed of all matters proposed for Bulletins. These matters may be included in the Board's agenda at the option of the Board. Technical Bulletins usually are not exposed, but may be at the option of the Staff.

Other

In addition, the Board may issue Invitations to Comment, Research Reports and booklets that help to illustrate Standards. None of these require prior exposure.

RECENT DEVELOPMENTS

Developments during the last five months include the reappointment of John W. March to a full five-year term. His new term will expire in December 1984. The FASB initiated a new series, FASB Technical Bulletins, to deal with implementation questions concerning other official financial accounting pronouncements. To date, nineteen Technical Bulletins have been issued; these deal with matters previously answered by the Staff in the form of private letters (see p. 46).


A Discussion Memorandum, *Effect of Rate Regulation on Accounting for Regulated Enterprises*, was issued on December 31, 1979 (see p. 64). The public hearing will be held in Chicago on May 28 and 29, 1980. A proposed Interpretation, *Applying FASB Statement No. 34 to Oil and Gas Producing Operations Accounted for by the Full Cost Method* was issued on January 28, 1980 (see p. 59). Various Interpretations, amendments, and Research Reports are in process (see pp. 69 and 70). Other items have been proposed to the FASB, but not yet placed on its agenda (see p. 71).
STATEMENTS OF FINANCIAL ACCOUNTING CONCEPTS ISSUED

Purpose and Authority

— The purpose of the series on concepts is to set forth objectives and fundamentals on which financial accounting and reporting standards will be based.

• The objectives identify the goals and purposes of financial reporting.

• The fundamentals are the underlying concepts of financial accounting.
  o Concepts guide the selection of transactions, events, and circumstances to be accounted for, their measurement and recognition, and the means of summarizing and communicating them to interested parties.

— Statements of Financial Accounting Concepts do not establish generally accepted accounting principles and, therefore, are not intended to invoke the application of Rule 203 or 204 of the AICPA Rules of Conduct of the Code of Professional Ethics.

— Pending reexamination of its pronouncements, as well as those of predecessor standard-setting bodies, and existing accounting practices in the light of the concepts developed, Statements of Financial Accounting Concepts do not require or justify:

• A change in existing accounting principles.

• Amendment, modification, or interpretation of existing standards of the Board and predecessor bodies.

• A change in existing accounting and reporting practices based on a personal interpretation of the objectives and concepts.

No. 1 — Objectives of Financial Reporting by Business Enterprises (November 1978)

— Establishes the objectives of general purpose external financial reporting by business enterprises.

• Does not conclude that the uses and objectives of financial reporting by other kinds of entities are, or should be, the same as or different from those of business enterprises.

• Contains no conclusions about matters such as the identity, number or form of financial statements, the attributes to be measured, or the unit of measure to be used.

• Objectives pertain to financial reporting, and are not restricted to information communicated by financial statements.
  o Financial reporting includes not only financial statements but also other means of communicating information that relates, directly or indirectly, to the information provided by the accounting system.

• Objectives are affected by the economic, legal, political, and social environment in the United States.

• Objectives are also affected by characteristics and limitations of the information that financial reporting, and particularly financial statements, can provide.
  o The information is primarily financial in nature — it is generally quantified and expressed in units of money.
  o The information is often limited by constraints inherent in procedures, such as verification, that are commonly used to enhance the reliability or objectivity of the information.
The information pertains to individual business enterprises, which may comprise two or more affiliated entities, rather than to industries or an economy as a whole.

The information often results from approximations of the financial effects of transactions and events, rather than exact measures. Numerous estimates, classifications, summarizations, judgments, and allocations are involved in the measurement process.

The information largely reflects the financial effects of transactions and events that have already happened.

Financial reporting is but one source of information needed to make economic decisions about business enterprises.

Financial information involves a cost to provide and use.

The objectives stem primarily from the informational needs of external users who lack the authority to prescribe the financial information they want from the enterprise and must use the information that management communicates to them.

For pragmatic reasons, the objectives are focused on information for investment and credit decisions.

Objectives

Financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions.

The information should be comprehensible to those who have a reasonable understanding of business and economic activities and are willing to study the information with reasonable diligence.

Financial reporting should provide information to help present and potential investors and creditors and other users in assessing the amounts, timing, and uncertainty of prospective cash receipts from dividends or interest and the proceeds from the sale, redemption, or maturity of securities or loans.

The prospects for those cash receipts are affected by an enterprise's ability to generate enough cash to meet its obligations when due and its other cash operating needs, to reinvest in operations, and to pay cash dividends, and may be affected by investors' and creditors' perceptions about that ability, which affects share market prices.

Financial reporting should, therefore, provide information to help investors, creditors, and others assess the amounts, timing, and uncertainty of prospective net cash inflows to the related enterprise.

Financial reporting should provide information about the economic resources of an enterprise, the claims to those resources (obligations of the enterprise to transfer resources to other entities and owners' equity), and the effects of transactions, events, and circumstances that change resources and claims to those resources.

The primary focus of financial reporting is information about an enterprise's performance provided by measures of earnings and its components.

Periodic earnings measurement involves relating to periods the benefits from, and the costs of, operations and other transactions, events, and circumstances that affect an enterprise.

Accrual accounting generally provides a better indication of enterprise performance than information about current cash receipts and payments.
• The goal of accrual and deferral of benefits and sacrifices is to relate the accomplishments and the efforts so that reported earnings measure an enterprise's performance during a period.

• Financial reporting should provide information about how an enterprise obtains and spends cash, about its borrowings and repayment of borrowings, about its capital transactions (including cash dividends and other distributions of enterprise resources to owners), and about other factors that may affect an enterprise's liquidity or solvency.

• Financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to management.
  o Earnings information is commonly the focus for assessing management’s stewardship or accountability.
  o Financial reporting and financial statements usually cannot, and do not, separate management performance from enterprise performance.

• Financial reporting should include explanations and interpretations to help users understand financial information provided.

The objectives leave unanswered the following topics which are to be the subject of other Statements of Financial Accounting Concepts:

• The identity, number, and form of financial statements.

• Elements of financial statements and their recognition, measurement and display.

• Information that should be provided by other means of financial reporting.

• Qualitative characteristics such as relevance, reliability and other criteria for evaluating and selecting accounting information.
STATEMENTS OF FINANCIAL ACCOUNTING STANDARDS ISSUED

No. 1 — Disclosure of Foreign Currency Translation Information (December 1973)
(Superseded by FASB Statement No. 8, Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements—October 1975)

No. 2 — Accounting for Research and Development Costs (October 1974)
— Requires that research and development costs be charged to expense when incurred.
— Disclosure is required in the financial statements of the total research and development costs charged to expense in each period for which an income statement is presented.
— Additional disclosures are required of regulated enterprises that defer research and development costs for financial statement purposes in accordance with the Addendum to APB Opinion No. 2.
— Effective for fiscal years beginning on or after January 1, 1975. Retroactive application by prior period adjustment is required.
— Interpreted by:
  • FASB Interpretation No. 4, Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method.
  • FASB Interpretation No. 6, Applicability of FASB Statement No. 2 to Computer Software.

No. 3 — Reporting Accounting Changes in Interim Financial Statements, an amendment of APB Opinion No. 28 (December 1974)
— If a cumulative-effect type accounting change is made in other than the first interim period, the cumulative effect of the change shall not be included in net income of the period of change.
  • Financial information for the pre-change interim periods of the fiscal year in which the change is made shall be restated by applying the newly adopted accounting principle.
  • The cumulative effect of the change on retained earnings at the beginning of the fiscal year shall be included in restated net income of the first interim period.
— Requires some publicly traded companies that make an accounting change in the fourth quarter (but that do not issue a separate fourth quarter report or disclose the quarterly effects of the change in their annual reports) to make the required disclosure in a note to their annual financial statements.
— Effective for accounting changes made in interim periods ending on or after December 31, 1974.

No. 4 — Reporting Gains and Losses from Extinguishment of Debt, an amendment of APB Opinion No. 30 (March 1975)
— Requires that aggregated gains and losses from extinguishment of debt, net of related income tax effect, be classified as an extraordinary item, irrespective of whether the extinguishment is early, at scheduled maturity, or later.
— Does not apply to gains or losses from cash purchases of debt made to satisfy current or future sinking-fund requirements.
— Applies to regulated enterprises in accordance with the Addendum to APB Opinion No. 2.
— Effective for extinguishments occurring after March 31, 1975. Retroactive application is encouraged, but not required.

No. 5 — Accounting for Contingencies (March 1975)
— An estimated loss from a loss contingency shall be charged to income only if both of the following conditions are met:
  • Information available prior to the issuance of the financial statements indicates that it is probable that an asset had been impaired or a liability had been incurred at the date of the financial statements.
  • The amount of the loss can be reasonably estimated.
— Loss contingencies not meeting those two conditions require only adequate disclosure when there is at least a reasonable possibility that a loss or an additional loss may have been incurred.
— "Self-insurance" and "catastrophe reserves" do not meet the above conditions.
— General or unspecified business risks (such as are provided for in reserves for contingencies) do not meet the conditions for accrual.
— Gain contingencies should not be credited to income because to do so would recognize income prior to realization.
— The Statement applies to regulated enterprises in accordance with the Addendum to APB Opinion No. 2.
— Effective for fiscal years beginning on or after July 1, 1975. Earlier application is encouraged. A change in accounting principle resulting from compliance with the Statement shall be reported in accordance with APB Opinion No. 20. The cumulative effect of the change on retained earnings at the beginning of the year in which the change is made shall be included in the net income of the year of change ("catch-up" adjustment).
— Amended by FASB Statement No. 11, Accounting for Contingencies—Transition Method.
— Interpreted by FASB Interpretation No. 14, Reasonable Estimation of the Amount of a Loss.

No. 6 — Classification of Short-Term Obligations Expected To Be Refinanced, an amendment of ARB No. 43, Chapter 3, Section A (May 1975)
— Certain short-term obligations shall be excluded from current liabilities if the enterprise intends to refinance the obligations on a long-term basis and the ability to consummate refinancing is demonstrated by:
  • The post-balance-sheet-date issuance of a long-term obligation or equity securities, or
  • A financing agreement entered into before the balance sheet is issued and
    o The agreement does not expire within one year (or operating cycle) from the balance sheet date, and is not cancellable by the lender,
    o No violation of any provision in the financing agreement exists, and
    o The lender is financially capable of honoring the agreement.
— Adequate disclosure of the agreement should be made.
— Effective as of December 31, 1975. Reclassification in financial statements for periods ending prior to December 31, 1975 is permitted but not required.

— Interpreted by FASB Interpretation No. 8, Classification of a Short-Term Obligation Repaid Prior to Being Replaced by a Long-Term Security.

No. 7 — Accounting and Reporting by Development Stage Enterprises (June 1975)

— Defines a development stage company as one that is devoting substantially all of its efforts to establishing a new business, and either has not begun its planned principal operations or has started such operations but has not had significant revenue from them.

— No special accounting is applicable to development stage companies, subsidiaries, divisions and other components, but the company should be identified as being in the development stage and certain additional disclosures should be given about cumulative development stage costs from inception.

— Effective for fiscal periods beginning on or after January 1, 1976. Earlier application is encouraged.

• After the effective date, statements for periods prior to the effective date shall be restated; any adjustments that may be necessary shall be accounted for by prior period adjustment.

— Interpreted by FASB Interpretation No. 7, Applying FASB Statement No. 7 in Financial Statements of Established Operating Enterprises.

No. 8 — Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements (October 1975)

— Specifies that, before translation, foreign financial statements that are to be included by consolidation, combination, or the equity method in an enterprise’s financial statements must be conformed to U.S. generally accepted accounting principles.

— Provides a method of translation that is similar to the monetary-nonmonetary method heretofore used in practice and the temporal method described in Accounting Research Study No. 12.

• Foreign currency transactions (other than forward exchange contracts) should be translated as follows:
  o Cash and amounts receivable or payable at the balance sheet date should be translated at the current rate.
  o Assets carried at current market value stated in a foreign currency shall be translated at the current rate.
  o All other amounts should be translated at the rate in effect at the transaction date (historical rate).
  o Unperformed forward exchange contracts should be translated at the current rate.

• Foreign currency financial statements should be translated as follows:
  o Cash and amounts receivable and payable should be translated at the current rate.
  o Other assets and liabilities (including deferred debits and credits) should be translated at:
    • Historical rates for those accounts carried at historical cost (past exchange prices). Averaging and approximation may be necessary when applying historical rates.
- Current rates for those accounts carried at current prices (market, replacement), or future prices (future exchanges).
- Deferred taxes, under certain circumstances, may be translated at the current rate.
  - Revenue and expenses should be translated at rates that would approximate the rate in effect had the individual transactions been translated into dollars at the date incurred (averages), except for revenue and expense items that relate to balance sheet items translated at historical rates (such as depreciation).

- Gains or losses resulting from the required translation procedures must be recognized as current income and not deferred, except that gains or losses on a forward exchange contract should be deferred when the contract is intended as a hedge of an identifiable foreign currency commitment.
- Disclosure of the aggregate exchange gain or loss included in determining net income for the period is required. If practicable, effects of exchange rate changes on revenue and earnings, other than exchange gains or losses, should be described and quantified.
- Financial statements may not be adjusted for a rate change that occurs after the date of the financial statements, although disclosure may be necessary if the rate change and its effect are significant.
- Effective for fiscal years beginning on or after January 1, 1976. Earlier application is encouraged.
- Financial statements for periods before the effective date should be restated, if practicable, to conform to the Statement. If restatement for all prior periods presented is not practicable, then the cumulative effect on retained earnings at the beginning of the earliest period restated shall be included in determining the net income of that period in accordance with APB Opinion No. 20.

- Amended by FASB Statement No. 20, Accounting for Forward Exchange Contracts.

- Interpreted by:
  - FASB Interpretation No. 15, Translation of Unamortized Policy Acquisition Costs by a Stock Life Insurance Company.
  - FASB Interpretation No. 17, Applying the Lower of Cost or Market Rule in Translated Financial Statements.

No. 9 — Accounting for Income Taxes—Oil and Gas Producing Companies, an amendment of APB Opinions Nos. 11 and 23 (October 1975) (Superseded by FASB Statement No. 19, Financial Accounting and Reporting by Oil and Gas Producing Companies—December 1977)

No. 10 — Extension of “Grandfather” Provisions for Business Combinations, an amendment of APB Opinion No. 16 (October 1975)

- The five-year limitation in the grandfather provisions contained in paragraph 99 of APB Opinion No. 16 and in certain AICPA Accounting Interpretations is eliminated.
- Effective on November 1, 1975.
No. 11 — Accounting for Contingencies—Transition Method, an amendment of FASB Statement No. 5 (December 1975)

— Specifies that for fiscal years beginning on or after July 1, 1975, FASB Statement No. 5 shall be applied retroactively to earlier periods if presented. If restatement for all prior periods presented is not practicable, the cumulative effect on the retained earnings at the beginning of the earliest period restated shall be included in determining the net income of that period in accordance with APB Opinion No. 20.

— Effective retroactively to the effective date of FASB Statement No. 5 except that financial statements issued prior to January 1, 1976 that were based on the original transition requirements in paragraph 20 of FASB Statement No. 5 are not required to comply with FASB Statement No. 11.

No. 12 — Accounting for Certain Marketable Securities (December 1975)

— Specifies that the carrying amount of a marketable equity securities portfolio shall be the lower of its aggregate cost or market value, determined at the balance sheet date.
  • The amount by which aggregate cost of the portfolio exceeds market value shall be accounted for as a valuation allowance.

— All marketable equity securities classified as current in the balance sheet shall be treated as a single portfolio for the consolidated entity; likewise, all marketable equity securities classified as noncurrent shall be treated as a separate portfolio for the consolidated entity. In the case of unclassified balance sheets, marketable equity securities shall be considered as noncurrent assets. The portfolios of marketable equity securities owned by an entity accounted for by the equity method (subsidiary or investee) shall not be combined with the portfolios of the consolidated entities.

— If there is a change in the classification of marketable equity securities, the lower of cost or market at the date of change shall become the new cost basis and any difference should be treated as a realized loss.

— All realized gains and losses and all changes in the valuation for a marketable equity securities portfolio included in current assets shall be included in the determination of net income of the period in which they occur. Accumulated changes in the valuation allowance for a portfolio included in noncurrent assets or in an unclassified balance sheet shall be included in the equity section of the balance sheet.

— Disclosure is required of aggregate cost and market value (for each segregated portfolio), gross unrealized gains and gross unrealized losses (for each portfolio), and net realized gain or loss included in the determination of net income. Other disclosures are also called for.

— Special provisions are given for certain industries having specialized accounting practices.

— The Statement does not apply to not-for-profit organizations, pension funds, and mutual life insurance companies.

— Effective for fiscal periods and interim periods ending on or after December 31, 1975.
  • If the initial application of the Statement requires the establishment of a valuation allowance for the current portfolio, the amount thereof shall be included in the determination of net income for that period. Similarly, in the initial establishment of a valuation allowance for the noncurrent portfolio, the amount thereof shall be reflected separately in stockholders’ equity as of the end of that fiscal period.
— Interpreted by:

- FASB Interpretation No. 11, *Changes in Market Value After the Balance Sheet Date.*
- FASB Interpretation No. 12, *Accounting for Previously Established Allowance Accounts.*
- FASB Interpretation No. 16, *Clarification of Definitions and Accounting for Marketable Equity Securities That Become Nonmarketable.*

**No. 13 — Accounting for Leases** (November 1976)

— Lease Classification

- Lessee—A lease is classified as a **capital lease** if it meets any one of the following four criteria; otherwise, it shall be classified as an operating lease:
  - The lease transfers title by the end of the lease term.
  - The lease contains a bargain purchase option.
  - Lease term is equal to 75% or more of the estimated economic life of the leased property. If the beginning of the lease term falls within the last 25% of the total estimated life including earlier use, this criterion shall not be used.
  - Present value of the minimum lease payments, excluding amounts representing payments of executory costs to be paid by the lessor, including any profit thereon, equals or exceeds 90% of the excess of the fair value of the leased property to the lessor over any related investment credit retained by the lessor and expected to be realized by him. This criterion is subject to the same exception as referred to immediately above.

- Lessor—A lease is classified as a **sales-type lease** or **direct financing lease,** whichever is appropriate, if it meets any one of the preceding four criteria and in addition meets both of the following criteria; otherwise, it shall be classified as an operating lease:
  - Collectibility is reasonably predictable.
  - No important uncertainties surround the amount of unreimbursable costs yet to be incurred by the lessor.

— Accounting and Reporting

- Lessee
  - Lessee records a capital lease as an asset and an obligation at the sum of:
    - the present value of minimum lease payments exclusive of executory costs, together with any profit thereon, and
    - the present value of the payment called for by the bargain purchase option, if any.
  - If the amount so determined exceeds the fair value of the leased property at the inception of the lease, the amount recorded as the asset and obligation shall be the fair value.
Discount rate to be used by a lessee for purposes of applying the 90% recovery rule and recording a capital lease is the lessor's rate of interest implicit in the lease if (1) the lessee knows that rate and (2) it is less than the lessee's incremental borrowing rate; otherwise, the lessee will use its incremental borrowing rate.

Leased assets capitalized under the criterion of transfer of title by the end of the lease term or existence of a bargain purchase option shall be amortized over the life of the asset as if owned. Otherwise, the leased asset shall be amortized over the lease term.

Assets recorded under capital leases and the accumulated amortization thereon shall be separately identified in the balance sheet or in footnotes thereto. Likewise, the obligation shall be separately identified in the balance sheet. Unless the amortization is included in depreciation and that fact is disclosed, the amortization charge shall be separately disclosed in the financial statements or notes thereto.

Disclosures with regard to capital leases include: gross assets recorded, classified by nature or function; future minimum lease payments at the balance sheet date, in the aggregate and for each of the five succeeding fiscal years, with separate deductions from the total for the amount representing executory costs and for the amount of the imputed interest necessary to reduce the net minimum lease payments to present value; and total contingent rentals actually incurred.

Disclosures with regard to operating leases include the following: future minimum rental payments at the balance sheet date, in the aggregate and for each of the five succeeding fiscal years; sublease rentals; rental expense, showing separately minimum rentals, contingent rentals, and sublease rentals; and a general description of leasing arrangements.

Lessor

For sales-type leases, the minimum rentals during the lease term, net of executory costs together with any profit thereon, plus the unguaranteed residual value accruing to the benefit of the lessor is the gross investment in the lease. The present value of the minimum lease payments discounted at the interest rate implicit in the lease is the sale amount. The cost of the property less the present value of the residual value plus the direct cost of negotiating the lease is charged to income. The difference between the gross investment and the present value of that figure is recorded as unearned income and amortized on an interest basis.

Accounting for direct financing leases is similar to that described for sales-type leases except that no profit on sales is recognized.

Disclosures with regard to sales-type and direct financing leases include: the components of the net investment (future minimum lease payments to be received less executory costs and accumulated allowance for uncollectible payments, the unguaranteed residual values accruing to the lessor, and unearned income) as of the date of each balance sheet presented, future minimum lease payments to be received for each of the five succeeding fiscal years as of the date of the latest balance sheet presented, and total contingent rentals included in income for each period for which an income statement is presented. For direct financing leases only, the amount of unearned income included in income to offset initial direct costs charged against income should also be disclosed for each period for which an income statement is presented. The above disclosures are applicable only to enterprises whose leasing activities are a significant part of their business.
Disclosures with regard to operating leases include: the minimum future rentals as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding fiscal years; the cost and carrying amount of property on lease or held for leasing, by major classes of property according to nature or function, and the amount of accumulated depreciation in total as of the latest balance sheet presented; and the total contingent rentals included in income for each period for which an income statement is presented. These disclosures are applicable only to enterprises whose leasing activities are a significant part of their business.

Enterprises whose predominant activity is leasing are required to give a general description of the lessor’s leasing arrangements.

In participations by third parties, the sale or assignment of a lease or property subject to a sales-type or direct financing lease shall not negate the original accounting. Profit or loss shall be recognized at the time of the transaction, except under certain circumstances. The sale of property subject to an operating lease shall not be treated as a sale if the seller retains substantial risks.

Special topics include:

- Accounting and reporting for subleases, renewals and extensions.
- Leases involving real estate composed of only land, of land and buildings, or of only part of a building.
- In their separate financial statements, leases between related parties are to be treated the same as leases with unrelated parties except in circumstances where the terms of the lease are significantly different from those in similar transactions between unrelated parties.
- Sale-and-leaseback transactions—any profit or loss on the sale shall be deferred and amortized (1), for capital leases, in proportion to the amortization of the assets and (2), for operating leases, in proportion to rental payments over the period of time the asset is expected to be used. However, when the fair value of the property at the time of the transaction is less than the undepreciated cost, a loss shall be recognized.
- Accounting and reporting for leveraged leases require the use of the “investment with separate phases” method.

Effective Date and Transition

- Applies to transactions and lease agreement revisions entered into on or after January 1, 1977 except where made pursuant to the terms of a written commitment made prior to that date. The disclosures called for in the Statement shall be included in financial statements for calendar years or fiscal years ending after December 31, 1976.
- If the Statement is not applied retroactively, disclosure of the effect on the balance sheet and income statement of retroactive application is required beginning with financial statements for the year ending December 31, 1977 and thereafter until years beginning after December 31, 1980.
- Financial statements for periods beginning after December 31, 1980 must include retroactive application of the Statement. Financial statements of earlier years presented for comparative purposes are to be restated at least as far back as December 31, 1976.

Amended by:

- FASB Statement No. 17, Accounting for Leases—Initial Direct Costs.
• FASB Statement No. 23, *Inception of a Lease*.
• FASB Statement No. 26, *Profit Recognition on Sales-Type Leases of Real Estate*.
• FASB Statement No. 27, *Classification of Renewals or Extensions of Existing Sales-Type or Direct Financing Leases*.
• FASB Statement No. 28, *Accounting for Sales With Leasebacks*.
• FASB Statement No. 29, *Determining Contingent Rentals*.

— Interpreted by:
• FASB Interpretation No. 19, *Lessee Guarantee of the Residual Value of Leased Property*.
• FASB Interpretation No. 21, *Accounting for Leases in a Business Combination*.
• FASB Interpretation No. 23, *Leases of Certain Property Owned by a Governmental Unit or Authority*.
• FASB Interpretation No. 24, *Leases Involving Only Part of a Building*.
• FASB Interpretation No. 26, *Accounting for Purchase of a Leased Asset by the Lessee During the Term of the Lease*.
• FASB Interpretation No. 27, *Accounting for a Loss on a Sublease*.


— Annual financial statements and financial statements for interim periods that are expressly described as presenting financial position, results of operations, and changes in financial position in conformity with generally accepted accounting principles shall include certain information relating to:

- The enterprise's operations in different industries.
- Its foreign operations.
- Its major customers.
- Its export sales.

— Industry segments shall be established by management by:

- Identifying the individual products and services from which the enterprise derives its revenue.
- Grouping the services by industry lines into industry segments.
- Selecting the industry segments that are significant with respect to the enterprise as a whole.
  - Reference may be made to outside classification sources such as the Standard Industrial Classification, although none by itself is suitable for purposes of this Statement.
  - Profit centers are the logical starting point for establishing segments.

— Reportable segments are those that satisfy one or more of the following criteria:

- Contribute 10% or more of the combined revenue.
Operating profit or loss is 10% or more of the greater of the:
  - combined operating profit of all segments that did not incur an operating loss, or
  - combined operating loss of all segments that did incur an operating loss.

Identifiable assets are 10% or more of combined identifiable assets of all segments.

Reportable segments shall represent at least 75% of the combined revenue from sales to unaffiliated customers of all industry segments.

Ten segments may be a practical upper limit.

Information to be presented by segment:
  - Revenue including transfers to other segments.
  - Operating profit or loss (which represents revenue less all direct and allocable operating expenses exclusive of revenue earned at the corporate level, general corporate expenses, interest expense, domestic and foreign income taxes, equity in income of investees, extraordinary items, and the like).
  - Identifiable assets, including direct and jointly-used assets; assets used for general corporate purposes are excluded.

Other disclosures include details as to depreciation, capital expenditures, equity in income of investees, and the effect of a change in accounting method.

Foreign operations:
  - In addition to information concerning industry segments, separate information shall be presented at a minimum for an enterprise's foreign operations, either in the aggregate or (if appropriate) by geographic area, if foreign operations contribute 10% or more of consolidated revenue or if the assets identifiable with the foreign operations are 10% or more of consolidated assets.
  - Sales, profit, and asset data to be presented are similar to those to be presented for industry segments.
  - Export sales are reportable if exports are 10% or more of total revenue from sales to unaffiliated customers.
  - If 10% or more of total enterprise revenue is derived from sales to a single customer, to domestic government agencies in the aggregate, or to foreign governments in the aggregate, that fact and the amount of revenue shall be disclosed.

Methods of presentation are specified.

Effective for fiscal years beginning after December 15, 1976 and for interim periods within those fiscal years.

Amended by:
  - FASB Statement No. 21, *Suspension of the Reporting of Earnings Per Share and Segment Information by Nonpublic Enterprises*.
No. 15 — Accounting by Debtors and Creditors for Troubled Debt Restructurings (June 1977)

— Establishes standards of financial accounting and reporting by the debtor and by the creditor for a troubled debt restructuring.

— A restructuring of a debt constitutes a troubled debt restructuring “if the creditor is compelled by economic or legal considerations related to the debtor’s financial difficulties to grant relief to the debtor that cannot meet its obligations on the debt.”

• Debt restructurings that are not troubled debt restructurings would continue to be accounted for under existing principles, including APB Opinion No. 26, Early Extinguishment of Debt.

— Troubled debt restructurings are divided into two broad groups:
  • Debtor transfers receivables, real estate, or other assets to the creditor or issues its stock to the creditor to satisfy the creditor’s claim.
  • Terms of the debt are modified to defer or reduce the cash payments the debtor is required to make to the creditor.

— Debtors and creditors account for the fair value of assets transferred and equity interests granted.
  • Debtor recognizes a gain and creditor recognizes a loss for the difference between fair value of the consideration transferred and the recorded amount of the debt satisfied.
  • Debtor would also recognize a gain or loss on the assets transferred if their fair values differ from their recorded amounts.

— Modification of the terms of continuing debt call for prospective treatment for the effects of such modifications as reduced interest expense or interest income to maturity, with one exception. If the total amounts to be paid or received (principal and interest) are less than the carrying amount of the payable, the debtor would record a gain and the creditor would record a loss to the extent of the difference. Thereafter, all cash payments should be accounted for as reductions of the carrying amount of debt or receivable, and no interest expense or interest income shall be recognized.

— Disclosure requirements by debtor and creditor are specified.

— Except for certain matters relating largely to disclosure, effective for troubled debt restructurings occurring after December 31, 1977. Certain disclosures in financial statements of creditors are required for fiscal years ending after December 15, 1977. Earlier application is encouraged but not required.

No. 16 — Prior Period Adjustments (June 1977)

— Restricts prior period adjustments.

— All items of profit and loss recognized during a period, including accruals of estimated losses from loss contingencies, shall be included in the determination of net income for that period except the following which shall be treated as prior period adjustments:
  • Correction of an error of a prior period.
  • Adjustments that result from realization of income tax benefits of preacquisition operating loss carryforwards of purchased subsidiaries.

— Effective for financial statements for fiscal years beginning after October 15, 1977. Earlier application is encouraged but not required. The Statement shall not be applied retroactively to previously issued annual financial statements.
No. 17 — Accounting for Leases—Initial Direct Costs, an amendment of FASB Statement No. 13 (November 1977)

— Modifies and clarifies the definition of “initial direct costs.”

• Initial direct costs are those costs incurred by the lessor that are directly associated with negotiating and consummating completed leasing transactions. Those costs include, but are not necessarily limited to, commissions, legal fees, costs of credit investigations, and costs of preparing and processing documents for new leases acquired. In addition, that portion of salespersons’ compensation, other than commissions, and the compensation of other employees that is applicable to the time spent in the activities described above with respect to completed leasing transactions shall also be included in initial direct costs. That portion of salespersons’ compensation and the compensation of other employees that is applicable to the time spent in negotiating leases that are not consummated shall not be included in initial direct costs. No portion of supervisory and administrative expenses or other indirect expenses, such as rent and facilities costs, shall be included in initial direct costs.

• The Board recognized that reasonable allocations based on estimates or on periodic statistical samples could be employed in determining initial direct costs.

— Effective for leasing transactions and lease agreement revisions entered into on or after January 1, 1978. The provisions shall be applied retroactively at the same time and in the same manner as the provisions of FASB Statement No. 13 are applied retroactively, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply this Statement retroactively.


— Eliminates the requirement to disclose segment information in interim-period financial statements.

— Effective December 1, 1977, retroactive to the effective date of FASB Statement No. 14.

No. 19 — Financial Accounting and Reporting by Oil and Gas Producing Companies (December 1977)

— Requires oil and gas producing companies to use a version of the “successful efforts” method of accounting for costs incurred in searching for and developing oil and gas reserves.

— Among the accounting requirements are the following:

• Mineral interests in properties are recorded as assets when acquired.

• All exploration costs except the costs of drilling exploratory wells are charged to expense when incurred.

• The costs of drilling exploratory wells, including exploratory-type stratigraphic test wells, are capitalized as “construction-in-progress” when incurred, to be charged to expense later if the well is determined not to have found proved reserves or to be reclassified as an amortizable asset if proved reserves are discovered.
If producible quantities of reserves are found by a well drilled offshore or in a remote area, but classification of those reserves as proved depends on whether additional exploratory wells find enough additional reserves to justify a major capital expenditure, such as for an offshore production platform or a trunk pipeline, the cost of drilling the well can be deferred as construction-in-progress as long as the additional exploratory drilling is under way or firmly planned.

- After discovery of reserves, costs incurred to drill all development wells, including development-type stratigraphic test wells, are capitalized as amortizable assets.
- After production begins, the capitalized acquisition, exploration, and development costs relating to reserves that were discovered are amortized, on a unit-of-production basis, as the reserves are produced. For amortization purposes, properties may be grouped in a field under certain conditions.
- Unproved properties that are held must be reviewed for impairment and, if called for, a loss must be recognized.

Supersedes FASB Statement No. 9, *Accounting for Income Taxes—Oil and Gas Producing Companies*.

- Comprehensive interperiod tax allocation by the deferred method, as described in APB Opinion No. 11, *Accounting for Income Taxes*, shall be followed by oil and gas producing companies for intangible drilling and development costs and other costs incurred that enter into the determination of taxable income and pretax accounting income in different periods.
- The possibility that statutory depletion in future periods will reduce or eliminate the amount of income taxes otherwise payable shall not be taken into account.

Disclosures required include quantities of proved reserves and proved developed reserves of oil and gas at the beginning and end of each year, and changes therein during the year. Disclosure is also required of costs for property acquisitions, exploration, development, and production or lifting.

Effective for financial statements for fiscal years beginning after December 15, 1978 and for interim periods within those fiscal years. Accounting changes adopted to conform to the provisions of the Statement should be made retroactively by restating the financial statements of prior periods.

Amended by FASB Statement No. 25, *Suspension of Certain Accounting Requirements for Oil and Gas Producing Companies*.

**No. 20 — Accounting for Forward Exchange Contracts**, an amendment of FASB Statement No. 8 (December 1977)

Amends paragraph 27 of FASB Statement No. 8 to provide a transition period during which an enterprise may enter into a forward contract to hedge an existing commitment that was entered into before the effective date of FASB Statement No. 8. For purposes of determining compliance with the conditions for deferral of a gain or loss, such a forward contract would be considered to have met the conditions of paragraph 27(a) if the life of the forward contract extends from a date prior to March 31, 1978 to the anticipated transaction date or a later date.
— Amends paragraph 27(b) of FASB Statement No. 8 to permit the deferral of a gain or loss on a portion of a forward contract in excess of the amount of the foreign currency commitment to the extent that such portion is intended to provide a hedge on an after-tax basis. A gain or loss so deferred shall be included as an offset to the related tax effects in the period in which such tax effects are recognized.

— Effective prospectively beginning January 1, 1978. Earlier application encouraged for financial statements not previously issued. Restatement of previously issued financial statements is prohibited.

No. 21 — Suspension of the Reporting of Earnings Per Share and Segment Information by Nonpublic Enterprises, an amendment of APB Opinion No. 15 and FASB Statement No. 14 (April 1978)

— Suspends the requirements of APB Opinion No. 15 and FASB Statement No. 14 in the financial statements of nonpublic enterprises, pending completion of a major project on financial statements and financial reporting that focuses, in part, on small and closely held enterprises.

• Defines a nonpublic enterprise as an enterprise other than one (a) whose debt or equity securities trade in a public market on a foreign or domestic stock exchange or in the over-the-counter market (including securities quoted only locally or regionally) or (b) that is required to file financial statements with the Securities and Exchange Commission.

  o The suspension applies to enterprises with a broad class of public participants (such as mutual associations, cooperatives, nonbusiness organizations, and partnerships) that otherwise meet the nonpublic definition.

  o An enterprise is no longer nonpublic when its financial statements are issued in preparation for the sale of securities in a public market.

• The suspension applies to a complete set of separately issued financial statements of a subsidiary, corporate joint venture, or other investee that is nonpublic as the term is used in the Statement.

• The Statement does not affect the disclosure of information about economic dependency, as discussed in Statement on Auditing Standards No. 6, when such disclosure may be necessary for a fair presentation.


No. 22 — Changes in the Provisions of Lease Agreements Resulting From Refundings of Tax-Exempt Debt, an amendment of FASB Statement No. 13 (June 1978)

— Reconciles an apparent inconsistency between FASB Statement No. 13, Accounting for Leases, and APB Opinion No. 26, Early Extinguishment of Debt, arising from refundings of tax-exempt debt, including advance refundings that are accounted for as early extinguishments of debt.
— Lessee accounting:

- If a change in the provisions of a lease results from a refunding by the lessor, including an advance refunding that is accounted for as an early extinguishment of debt, the lessee shall adjust the lease obligation and recognize any gain or loss currently.
  - The difference between the present value of the future minimum lease payments using the effective interest rate applicable to the revised agreement and the present balance of the obligation is the measure of gain or loss.

- If the advance refunding is not accounted for as an early extinguishment of debt and the lessee is obligated to reimburse the lessor for any costs related to the debt to be refunded (such as unamortized discount or issue costs or a call premium), the lessee shall accrue those costs by the "interest" method over the period from the date of the advance refunding to the call date of the debt to be refunded.

— Lessor accounting:

- If a change in the provisions of a lease results from a refunding, including an advance refunding that is accounted for as an early extinguishment, the lessor shall adjust the balance of the minimum lease payments receivable and the estimated residual value, if affected (i.e., the gross investment in the lease), in accordance with the requirements of paragraphs 17 and 18 of Statement No. 13.
  - The adjustment of unearned income shall be the amount required to adjust the net investment in the lease to the sum of the present values of the two components of the gross investment based on the interest rate applicable to the revised lease agreement.
  - The sum of the adjustments of the gross investment and of unearned income shall be recognized as a gain or loss in the current period.

- If the advanced refunding is not accounted for as an early extinguishment of debt, the lessor shall systematically recognize, as revenue, any reimbursements to be received from the lessee for costs related to the debt to be refunded over the period from the date of the advance refunding to the call date of the debt to be refunded.

— Effective for lease agreement revisions entered into on or after July 1, 1978. The provisions of this Statement shall be applied retroactively at the same time and in the same manner as the provisions of Statement No. 13 are applied retroactively, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply this Statement retroactively.

No. 23 — Inception of the Lease, an amendment of FASB Statement No. 13 (August 1978)

— Reconsiders the application of FASB Statement No. 13, Accounting for Leases, for a leasing transaction in which the lessor and lessee agree on lease terms prior to the construction of the asset to be leased.

— "Inception of the lease" is defined as the date of the lease agreement or an earlier commitment.

- A preliminary agreement or commitment where any of the principal provisions are yet to be negotiated does not qualify for purposes of this definition.

— The "fair value of the leased property at the inception of the lease" is to reflect any increases in construction or acquisition cost of the leased property due to a cost-based or similar construction period escalator clause.
— The estimated residual value used to compute the unguaranteed residual value accruing to the benefit of the lessor shall not exceed the amount estimated at the inception of the lease adjusted for the effect of any increases in acquisition or construction cost of the leased property required by a cost-based or similar construction period escalator clause.

— Effective for leasing transactions recorded and lease agreement revisions recorded as of December 1, 1978 or thereafter. The provisions of the Statement shall be applied retroactively at the same time and in the same manner as the provisions of Statement No. 13, except that entities that have already applied Statement No. 13 retroactively in published annual financial statements need not apply this Statement retroactively.


— Eliminates the requirement to disclose segment information in a complete set of financial statements that is presented in another enterprise’s financial report (i.e., the primary reporting enterprise):

• If those financial statements are also consolidated or combined in a complete set of financial statements and both sets of financial statements are presented in the same financial report, or

• If those financial statements are presented for certain foreign investees, or

• If those financial statements are presented in the financial report of an enterprise that is not subject to the requirements of FASB Statement No. 14 because of the suspension provided by FASB Statement No. 21 relating to nonpublic enterprises.


No. 25 — Suspension of Certain Accounting Requirements for Oil and Gas Producing Companies, an amendment of FASB Statement No. 19 (February 1979)

— Suspends the effective date for application of those portions of FASB Statement No. 19, Financial Accounting and Reporting by Oil and Gas Producing Companies, that pertain to a required form of successful efforts accounting.

• Does not suspend those same portions of Statement No. 19 insofar as they provide definition of terms or provide direction and guidance for financial statement disclosures required by other portions of that Statement.

• Statement No. 19 continues in effect as a Statement issued by the FASB for purposes of justifying a change in accounting method under APB Opinion No. 20, Accounting Changes.

  o Accounting changes to adopt the provisions of Statement No. 19 shall be made by retroactive restatement of prior periods as provided for in that Statement.

— Enterprises that presently use a full cost method and subsequently adopt accounting changes to conform to the full cost rules promulgated by the Securities and Exchange Commission (SEC) shall make those changes retroactively by restating prior-period financial statements.
— Disclosure requirements of Statement No. 19 are amended to permit the disclosure of reserve quantities to be made as supplementary information accompanying, but outside, the financial statements.

— Definitions of proved reserves, proved developed reserves and proved undeveloped reserves used in applying this Statement and Statement No. 19 shall be the definitions adopted by the SEC.

• Definitions of reserves provided in Statement No. 19 are rescinded.
• Previously reported quantities of various reserves shall not be revised retroactively if the SEC definitions are changed.

— An enterprise engaged in oil and gas producing activities shall disclose the method of accounting for the costs incurred in those activities and the manner of disposing of capitalized costs related to those activities.

— For all other purposes, the effective date of Statement No. 19 is amended to fiscal years ending after December 25, 1979, although prior application is encouraged.

• The suspension, as a mandatory requirement, of the form of successful efforts accounting prescribed by Statement No. 19 is an indefinite suspension.


No. 26 — Profit Recognition on Sales-Type Leases of Real Estate, an amendment of FASB Statement No. 13 (April 1979)

— Amends paragraph 8 of FASB Statement No. 13 to require that a lease involving real estate that would otherwise be classified as of the inception date as a sales-type lease giving rise to a manufacturer’s or dealer’s profit shall be classified as an operating lease unless at the beginning of the lease term it also meets the requirements that a sale of the same property would have to meet for full and immediate profit recognition under the AICPA Industry Accounting Guide, Accounting for Profit Recognition on Sales of Real Estate.

• The accounting guide’s requirements relate to the adequacy of the buyer’s initial and continuing investment in the property acquired, and the conditions relating to the seller’s continued involvement with the property sold.

— Effective for leasing transactions, and lease agreement revisions, recorded as of August 1, 1979 or thereafter. The provisions shall be applied retroactively at the same time and in the same manner as the provisions of FASB Statement No. 13 are applied retroactively, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply this Statement retroactively.

No. 27 — Classification of Renewals or Extensions of Existing Sales-Type or Direct Financing Leases, an amendment of FASB Statement No. 13 (May 1979)

— Modifies FASB Statement No. 13, Accounting For Leases, to require the classification of a renewal or extension of an existing sales-type or direct financing lease as a sales-type lease if it would otherwise so qualify, and the renewal or extension occurs at or near the end of the original lease term.

— Effective for lease agreement renewals and extensions recorded as of September 1, 1979 or thereafter. The provisions shall be applied retroactively at the same time and in the same manner as the provisions of Statement No. 13 are applied retroactively, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply this Statement retroactively.
No. 28 — Accounting for Sales With Leasebacks, an amendment of FASB Statement No. 13 (May 1979)

— Modifies paragraph 33 of FASB Statement No. 13, Accounting for Leases, to allow for recognition of profit on a sale and leaseback under certain circumstances.

• Profit or loss on a sale and leaseback should be recognized if the seller-lessee relinquishes the right to substantially all of the remaining use of the property sold, retaining only a minor portion of such use.
  o A minor portion is defined operationally to represent situations in which the present value of the leaseback represents 10% or less of the fair value of the asset sold.
  o If the amount of rentals called for by the lease is unreasonable under current market conditions, an appropriate amount of profit or loss on the sale shall be deferred and amortized to adjust rentals to a reasonable amount.

• If the seller-lessee realizes a profit in excess of the present value of the minimum lease payments on an operating lease, or the recorded amount of the leased asset on a capital lease, profit in the amount of the excess shall be recognized at the date of the sale.

• If the fair value of the property at the time of the transaction is less than its undepreciated cost, a loss shall be recognized immediately up to the amount of the difference.

— Modifies paragraph 33 of FASB Statement No. 13 to require that, for an operating lease where profit or loss is deferred, it be amortized over the lease term, not the period of expected use.

— Effective for leasing transactions and lease agreement revisions recorded as of September 1, 1979. Provisions of this Statement shall be applied retroactively at the same time and in the same manner as the provisions of Statement No. 13 are applied retroactively, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply this Statement retroactively.

No. 29 — Determining Contingent Rentals, an amendment of FASB Statement No. 13 (June 1979)

— Modifies FASB Statement No. 13, Accounting For Leases, to exclude contingent rentals, as defined, from minimum lease payments.

• Contingent rentals are increases or decreases in lease payments that result from changes, occurring subsequent to the inception of the lease, in factors (other than the passage of time) on which lease payments are based.

• Exceptions to the definition are as follows:
  o Escalation relating to increases in the construction or acquisition cost of the leased property, or for increases in some measure of cost or value during the construction or pre-construction period, shall be excluded from contingent rentals.
  o Lease payments that depend on an existing index or rate shall be included in minimum lease payments based on the index or rate existing at the inception of the lease. Increases or decreases in payments that result from subsequent changes in the index or rate are contingent rentals.
No. 30 — Disclosure of Information About Major Customers, an amendment of FASB Statement No. 14 (August 1979)

- Amends the requirements of paragraph 39 of FASB Statement No. 14, Financial Reporting for Segments of a Business Enterprise, regarding disclosure of revenue derived from a single customer accounting for 10% or more of total sales.
  - For purposes of disclosure, the federal government, a state government, a local government (for example, a county or municipality) or a foreign government shall each be considered as a single customer.
  - The identity of the customer need not be disclosed, but the identity of the industry segment or segments making the sales shall be disclosed.

- Effective for fiscal years beginning after December 15, 1979. The Statement need not be applied retroactively to previously issued financial statements.

No. 31 — Accounting for Tax Benefits Related to U.K. Tax Legislation Concerning Stock Relief (September 1979)

- Specifies how an enterprise reporting in accordance with U.S. GAAP should account for the tax effects related to the provisions of the 1979 United Kingdom (U.K.) tax legislation concerning recapture of "stock (inventory) relief" deductions.

- Background:
  - For purposes of determining U.K. taxable income, enterprises are permitted to deduct increases in the carrying amount of inventories. This deduction is included in U.K. taxable income (recaptured) if inventories decrease in future years.
  - Tax benefits relating to this deduction have been deferred as if this deduction were a timing difference that reverses if inventories decrease in future years.
  - Effective on July 26, 1979, the U.K. adopted legislation that limits the timing and the amount of tax that could be recaptured.

- The tax benefit related to the current deductions for "stock relief" should be deferred unless it is probable that the tax benefit will not be recaptured prior to the end of the relevant six-year recapture period.

- Previously provided deferred tax benefits related to "stock relief" deductions should be recognized in the earliest of the period in which the recapture period expires or the period in which circumstances change and it becomes probable that the tax benefits will not be recaptured.

- If the tax benefit related to "stock relief" has not been deferred and circumstances subsequently change, the tax benefit attributable to the "stock relief" shall be deferred to the extent appropriate by a charge to income tax expense of the period in which circumstances change.

- For interim reporting purposes, except for purposes of initial application, any change in circumstances requiring an adjustment of the tax benefit related to "stock relief" should be treated as an adjustment of the estimated annual effective tax rate.
— If a significant variation in the customary relationship between income tax expense and pretax accounting income is created by accounting for “stock relief” in accordance with the statement, that fact shall be disclosed.

— Effective for annual and interim financial statements issued after September 30, 1979 for periods ending on or after July 26, 1979. For initial application of the Statement in interim periods ending after July 26, 1979, any recognition of previously deferred tax benefits related to “stock relief” should be reported as an item of tax expense for that interim period.

No. 32 — Specialized Accounting and Reporting Principles and Practices in AICPA Statements of Position and Guides on Accounting and Auditing Matters, an amendment of APB Opinion No. 20 (September 1979)

— Adopts the specialized accounting and reporting principles and practices contained in the AICPA Industry Accounting Guides, Industry Audit Guides, and Statements of Position, listed in Appendix A of the Statement as preferable accounting principles for purposes of applying APB Opinion No. 20, Accounting Changes.

• Defers action on the Industry Audit Guide, Audits of State and Local Governmental Units, and two related SOPs pending completion of discussions on the role of the FASB in accounting for governmental units.

• Special procedures are established for adopting SOPs and Guide revisions in process.

— Does not require any enterprise to change the accounting principles it currently uses to those specified in the Guides and SOPs.

• Does not take any position with respect to the initial adoption of an accounting principle prior to completion of appropriate due process on the specialized principles and practices.

— Effective October 31, 1979. Earlier application is encouraged.

— At its October 31, 1979 meeting, the Board approved the use of task forces to extract the specialized accounting and reporting principles and practices for preparation of Exposure Drafts of proposed Standards on these AICPA Statements of Position and Guides.

No. 33 — Financial Reporting and Changing Prices (September 1979)

— Establishes standards for reporting the effects on business enterprises of changes in general prices (general inflation) and changes in the prices of certain specific types of assets (current costs).

• Requires that the effects of changing prices be presented as supplementary information to the primary financial statements.

  o The effects of general inflation are measured by the use of constant dollar accounting, a method of reporting financial statement elements in dollars each of which has the same general purchasing power.

  o The effects of changes in the prices of specific types of assets are determined through the use of current cost accounting, a method of reporting assets, and expenses associated with the use or sale of assets, at their current cost or lower recoverable amount at the balance sheet date or at the date of use or sale.

• No changes are made in the primary financial statements.
— Applicable to U.S. public enterprises, as defined in the Statement, that prepare their primary financial statements in U.S. dollars and in accordance with U.S. generally accepted accounting principles and that, at the beginning of the fiscal year for which financial statements are being presented (on a consolidated basis, if applicable), meet either of the following two conditions:

- Inventories and property, plant, and equipment (before deducting accumulated depreciation, depletion, and amortization) amount in the aggregate to more than $125 million;
  - Inventory and property, plant, and equipment includes land, other material resources and capitalized leases, but not goodwill or other intangible assets.
- Total assets amount to more than $1 billion (after deducting accumulated depreciation).

— The information need not be presented:

- In interim financial reports,
- For segments of a business, or
- For a parent company, an investee company, or other enterprise in any financial report that includes the results for that enterprise in consolidated financial statements.

— Special problems in the forest products, mining, oil and gas, and real estate industries require further study to provide a basis for implementing the requirements of current cost disclosure.

- Pending completion of these studies, enterprises are not required to disclose information about the current costs of unprocessed natural resources and income-producing real estate properties.

— Required disclosures for the current year include the following information:

- Income from continuing operations on an historical cost/constant dollar basis and on a current cost basis.
  - Income from continuing operations excludes the results of discontinued operations, extraordinary items, and the cumulative effect of accounting changes.
- Purchasing power gain or loss on net monetary items.
- Current cost amounts of inventory and property, plant and equipment.
- Increases or decreases in the current cost amounts of inventory and property, plant and equipment held during the period net of inflation (holding gains or losses net of inflation).

- Additional information required includes disclosure of:
  - The types of information used to calculate the current cost of inventory, property, plant and equipment, cost of goods sold, and depreciation, depletion, and amortization expense.
  - Any differences from the primary statement in depreciation methods, estimates of useful lives, and salvage values used for purposes of the supplementary disclosure.
  - The fact that no adjustments were made to income tax expense as reported in the primary financial statements.
— Required disclosures for each of the five most-recent fiscal years. These disclosures include:

- **Historical cost/constant dollar information:**
  - Net sales and other operating revenues.
  - Income from continuing operations.
  - Income per share from continuing operations.
  - Net assets at fiscal year end.
  - Cash dividends declared per common share.

- **Current cost information:**
  - Income from continuing operations.
  - Income per common share from continuing operations.
  - Net assets at fiscal year end.
  - Increases or decreases in the current cost amounts of inventory and property, plant and equipment, net of inflation.
  - Purchasing power gain or loss on net monetary items.

- **Other:**
  - Market price per common share at fiscal year end.
  - The average level (or end-of-year-level, if used for the measurement of income from continuing operations) of the Consumer Price Index for All Urban Consumers (CPI-U) for each year included in the summary.

The index used to compute information on a constant dollar basis is the CPI-U.

- An enterprise that presents the minimum historical cost/constant dollar information required must use, for restatement purposes, the average level over the fiscal year of the CPI-U.
  - Minimum restatement covers inventory, property, plant and equipment, cost of goods sold, depreciation, depletion, and amortization expense, and any reductions of the historical cost amounts of inventory and property, plant, and equipment to lower recoverable amounts.
  - Other financial statement elements need not be restated.

- An enterprise that presents *comprehensive* financial statements on an historical cost/constant dollar basis may measure the components in either average-for-the-year constant dollars or in end-of-year constant dollars.

— Items measured in units of a foreign currency shall first be translated into U.S. dollars in accordance with generally accepted accounting principles and then be restated in constant dollars.

— Guidance is provided on the classification of balance sheet items as monetary or non-monetary.

— Details are provided for such matters as current cost measurements and sources of information about current costs.
— If the recoverable amount for a group of assets is judged to be materially and permanently lower than historical cost in constant dollars or current dollars, the recoverable amount must be used as the measure of the asset and related expense.

• Recoverable amounts may be measured by considering net realizable value or the values in use of the assets.

• Special rules apply to companies subject to rate regulation or other forms of price control.

— Effective for fiscal years ended on or after December 25, 1979.

• Information on a current cost basis for fiscal years ended before December 25, 1980 may be presented in the first annual report for a fiscal year that ends on or after December 25, 1980.

• Of the above information, only the following information need be stated in the five-year summary for fiscal years ended before December 25, 1979:
  o Net sales and other operating revenues.
  o Cash dividend declared per common share.
  o Market price per common share at fiscal year end.

• Disclosures of current cost information in the five-year summary for fiscal years ending before December 25, 1980 may be postponed to the first annual report for a fiscal year ending on or after December 25, 1980.

• An enterprise that first applies the requirements for a fiscal year ended on or after December 25, 1980 is required to state in the five-year summary for earlier years the following, in constant dollars:
  o Net sales and other operating revenues.
  o Cash dividend declared per common share.
  o Market price per common share at fiscal year end.

— Illustrations of Financial Reporting and Changing Prices (December, 1979)

• Issued as a supplement to FASB Statement No. 33, it contains illustrations that might be appropriate in annual reports of companies in particular industries.

No. 34 — Capitalization of Interest Cost (October 1979)

— Establishes standards of financial accounting and reporting for capitalizing interest cost as a part of the historical cost of acquiring certain assets.

• Interest cost includes interest recognized on obligations having explicit interest rates, interest imputed on payables in accordance with APB Opinion No. 21, Interest on Receivables and Payables, and interest relating to a capital lease.

• Interest that might be imputed on owners' equity is excluded.

— Interest cost shall be capitalized as part of the historical cost of acquiring an asset if a significant period of time elapses between the initial expenditure related to development of the asset and its readiness for its intended use, and if such a period of time is required to bring the asset to the condition and location necessary for its intended use.
Assets qualifying for interest capitalization include:

- Assets that are constructed or otherwise produced for an enterprise’s own use.
- Assets intended for sale or lease that are constructed or otherwise produced as discrete projects, such as ships or real estate developments.

Interest should not be capitalized for the following:

- Inventories that are routinely manufactured or otherwise produced in large quantities on a repetitive basis.
- Assets that are in use or ready for their intended use.
- Assets that are not being used in the earning activities of the enterprise.

The amount of interest cost allocated in an accounting period shall be determined by applying an interest rate to the average amount of accumulated expenditures for the qualified asset during the period, and shall not exceed the amount of total interest cost incurred by the enterprise during that period.

- If an enterprise’s financial plans associate a specific new borrowing with a qualifying asset, the enterprise may use the rate on that borrowing as the capitalization rate.

- If the average accumulated expenditures for the asset exceed the amounts of specific new borrowings associated with the asset, the capitalization rate to be allocated to the excess shall be the weighted average of the rates applicable to other borrowings.

- The relevant enterprise for interest capitalization is the enterprise for which financial statements are presented. A consolidated group of companies may be viewed as a single entity for financing purposes.

Capitalization begins when the first development expenditure is made, and continues as long as the asset is undergoing active development that is necessary to get the asset ready for its intended use, and interest is being incurred. Interest capitalization shall end when the asset is substantially complete and ready for its intended use.

The following disclosures are required:

- For an accounting period in which no interest cost is capitalized, the amount of interest cost incurred and charged to expense during the period.

- For an accounting period in which some interest cost is capitalized, the total amount of interest cost incurred during the period and the amount thereof that has been capitalized.

Shall be applied prospectively in fiscal years beginning after December 15, 1979. Earlier application is permitted, but not required in financial statements for fiscal years beginning before December 19, 1979 that have not been previously issued. If early application is adopted, financial reports for any interim periods of that fiscal year that precede the period of adoption shall be restated.
No. 35 — Accounting and Reporting by Defined Benefit Pension Plans (March 1980)

— Establishes standards of financial accounting and reporting for annual financial statements of defined benefit pension plans, and applies to plans that are subject to the provisions of ERISA (covered plans) as well as to those that are not.

- Covered plans may additionally provide benefits on death, disability, or termination of employment.
- Does not apply to a plan that is expected to be terminated, nor to a government-sponsored social security plan.

— This Statement does not require the preparation, distribution, or attestation of any plan’s financial statements.

— The primary objective of a plan’s financial statements is to provide financial information that is useful in assessing a plan’s present and future ability to pay benefits when due.

— The annual financial statements of a plan shall include the following:
  - A statement that includes information on the net assets available for benefits as of the end of the plan year.
  - A statement that includes information on changes during the year in net assets available for benefits.
  - Information on the actuarial present value of accumulated plan benefits:
    - The benefit valuation date may be either the beginning or the end of the plan year.
    - If the benefit valuation date is the beginning of the year, then a statement of net assets available at that date and of changes in net assets during the preceding year should be presented.
  - Information on the effects of factors affecting the year-to-year change in the actuarial present value of accumulated plan benefits.
  - Flexibility is allowed in presenting information regarding the actuarial present value of accumulated plan benefits, and year-to-year changes therein.

— Accounting principles set forth in the Statement include the following:
  - Accrual basis of accounting is required.
  - Contributions receivable shall include all amounts legally or contractually due as well as amounts due pursuant to formal commitments.
  - Plan investments, whether equity or debt securities, real estate, or other (excluding contracts with insurance companies) shall be presented at their fair value (i.e., current selling price) at the reporting date.
  - Insurance contracts shall be recognized and measured in the same manner as required for reporting under ERISA.
  - Operating assets shall be presented at cost less accumulated depreciation.

— Minimum disclosure requirements are set forth for changes in net assets available for benefits.

— Accumulated plan benefits are those future benefit payments that are attributable under the plan’s provisions to employees’ service rendered to the benefit information date.
• Accumulated plan benefits comprise benefits expected to be paid to:
  o Retired or terminated employees or their beneficiaries.
  o Beneficiaries of deceased employees.
  o Present employees or their beneficiaries.
• Specific rules are provided for measuring accumulated plan benefits.
• Changes in actuarial assumptions made to reflect changes in the plan’s expected experience shall be viewed as changes in estimate.
• Minimum disclosure shall include the significant effects of factors affecting a change in the actuarial present value of accumulated plan benefits, such as:
  o Plan amendments.
  o Changes in the nature of the plan (such as a plan spinoff or a merger with another plan).
  o Changes in actuarial assumptions.
• Total actuarial present value of accumulated plan benefits as of the benefit information date shall be segmented into at least the following categories:
  o Vested benefits of participants currently receiving payments
  o Other vested benefits
  o Nonvested benefits
— The use of averages or other methods of approximation is appropriate provided the results are substantially the same as would be obtained under detailed rules.
— Disclosures specifically related to plans are set forth in detail.
— Effective for plan years beginning after December 15, 1980.
• Accounting changes to conform to this Statement shall be made retroactively.
• Prior years’ statements when presented for comparative purposes shall be restated.
• If accounting changes were necessary to conform to the provisions of this Statement, that fact shall be disclosed.
INTERPRETATIONS ISSUED

No. 1 — Accounting Changes Related to the Cost of Inventory, an interpretation of APB Opinion No. 20 (June 1974)

— A change in composition of the elements of costs included in inventory is an accounting change and a company making such a change should conform with APB Opinion No. 20, including justifying the change as to preferability determined on the basis of whether the new principle constitutes an improvement in financial reporting and not on the basis of income tax effect alone.

— Effective July 1, 1974.

No. 2 — Imputing Interest on Debt Arrangements Made Under the Federal Bankruptcy Act, an interpretation of APB Opinion No. 21 (June 1974) (Superseded by FASB Statement No. 15, Accounting by Debtors and Creditors for Troubled Debt Restructurings — June 1977)

No. 3 — Accounting for the Cost of Pension Plans Subject to the Employee Retirement Income Security Act of 1974, an interpretation of APB Opinion No. 8 (December 1974)

— No change in the minimum or maximum limits for the annual provision for pension costs set forth in APB Opinion No. 8 is required as a result of the Act, although the actual amount charged may be changed.

— Any significant estimated effect on the future amount of an enterprise’s periodic provision for pension expense, periodic funding of pension costs, or unfunded vested benefits shall be disclosed in the notes.

— At present the Board does not believe the Act creates a legal obligation for unfunded pension costs that warrants accounting recognition of a liability pursuant to APB Opinion No. 8, unless a plan is terminated.

— Effective December 31, 1974.

No. 4 — Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method, an interpretation of FASB Statement No. 2 (February 1975)

— FASB Statement No. 2 specifies that research and development costs be expensed. Interpretation No. 4 clarifies the accounting treatment to be given when research and development is acquired through a purchase business combination.

  • The fair value of the research and development of the acquired enterprise must be determined and suitable allocation of the purchase price made.
    ○ Those costs allocated to research and development that are to be used by the acquiring company for research and development purposes (as defined in FASB Statement No. 2) must then be written off to income.
    ○ Those costs allocated to research and development which will not be used by the acquiring company for research and development purposes, or which have alternative future use, may remain capitalized and be amortized over a suitable period.
    ○ Costs incurred under a contract to resell are not subject to FASB Statement No. 2.
  • Adequate disclosure of research and development costs acquired through a purchase business combination must be given.
— Effective for combinations initiated after March 1, 1975. Application to combinations initiated prior to April 1, 1975 and consummated after March 1, 1975 is encouraged but not required. Retroactive application is not required.

No. 5 — Applicability of FASB Statement No. 2 to Development Stage Enterprises, an interpretation of FASB Statement No. 2 (February 1975) (Superseded by FASB Statement No. 7, Accounting and Reporting by Development Stage Enterprises — June 1975)

No. 6 — Applicability of FASB Statement No. 2 to Computer Software, an interpretation of FASB Statement No. 2 (February 1975)

— FASB Statement No. 2 specifies that costs of certain computer software programs and procedures are research and development costs. Interpretation No. 6 provides guidelines for determining which computer costs are research and development costs pursuant to FASB Statement No. 2 and, therefore, must be expensed as incurred.

• Costs incurred to purchase or lease computer software developed by others are research and development costs if the software is to be used in research and development activities of the acquiring enterprise, and therefore, they must be expensed as incurred.

• Costs incurred in development of software are research and development costs if the software is used for developing or significantly improving a product or process (including the software package) that is intended to be sold, leased or otherwise marketed, and therefore, they must be expensed as incurred.

NOTE: FASB Statement No. 2 does not specify any accounting for costs that are deemed not to be research and development. Accounting for all such costs must, therefore, be in accordance with other authoritative literature and GAAP. It follows that each of those costs may or may not be capitalized. For example, computer software costs that are deemed to be general and administrative costs would be expensed as incurred.

— Effective for fiscal years beginning on or after April 1, 1975 although earlier application is encouraged.

No. 7 — Applying FASB Statement No. 7 in Financial Statements of Established Operating Enterprises, an interpretation of FASB Statement No. 7 (October 1975)

— Explains the applicability of FASB Statement No. 7 to an established operating enterprise’s financial statements that include the financial statements of a development stage subsidiary or other investee.

— FASB Statement No. 7 does not address and does not alter GAAP for the preparation of consolidated financial statements. Therefore, the Statement does not address the question of whether a change in principle adopted in the separate statements of a development stage subsidiary to conform to FASB Statement No. 7 must be reflected in the consolidated statements.

— Capitalization or deferral of costs shall be subject to the same assessment of recoverability according to FASB Statement No. 7. This does not require that the results of the assessment must necessarily be the same. The Statement does not affect any accepted practice in consolidation of financial statements where the results of an assessment of recoverability of a cost may be different (a) in the broader context of a consolidated enterprise and (b) in the context of a development stage subsidiary standing alone.
— Except in circumstances described above, the effect of a development stage subsidiary’s change in accounting principle to conform its accounting to the requirements of FASB Statement No. 7 generally would be reflected in the consolidated statements.

— Consolidated statements for periods prior to the effective date of Statement No. 7 shall be restated by prior period adjustment for such matters.

— Effective for fiscal periods beginning on or after January 1, 1976, although earlier application is encouraged.

No. 8 — Classification of a Short-Term Obligation Repaid Prior to Being Replaced by a Long-Term Security, an interpretation of FASB Statement No. 6 (January 1976)

— FASB Statement No. 6 specifies that a short-term obligation is to be excluded from current liabilities only if the enterprise intends to refinance it on a long-term basis and, before the balance sheet is issued, either has refinanced it or has entered into a financing agreement that permits refinancing on a long-term basis.

— This Interpretation holds that, where a short-term obligation is repaid after the balance sheet date and subsequently a long-term obligation or equity securities are issued whose proceeds are used to replenish current assets before the balance sheet is issued, the short-term obligation shall not be excluded from current liabilities at the balance sheet date.

— Effective on February 29, 1976 and applies to balance sheets dated on or after that date and to related statements of changes in financial position.

No. 9 — Applying APB Opinions No. 16 and 17 When a Savings and Loan Association or a Similar Institution Is Acquired in a Business Combination Accounted for by the Purchase Method, an interpretation of APB Opinions Nos. 16 and 17 (February 1976)

— Acquisition of a savings and loan association in a business combination accounted for by the purchase method shall be accounted for under the separate-valuation [of individual (or types of) assets and liabilities] method following paragraphs 87 and 88 of APB Opinion No. 16.

— Use of the net-spread method ignores fair value of individual (or types of) assets and liabilities and is, therefore, inappropriate under APB Opinion No. 16. (In the net-spread method, the acquisition of a savings and loan association is viewed as the acquisition of a leveraged whole rather than the acquisition of the separate assets and liabilities and, therefore, its mortgage loan portfolio and savings accounts are brought forward at the net carrying amount shown in the financial statements of the acquired association.)

— The purchase price may include an amount for special savings and loan factors (such as capacity to generate future income, new business, or nature of territory). The amount paid for separately identified intangible assets shall be recorded as the cost of the intangible and be amortized over its estimated life as specified in APB Opinion No. 17.

— Permits amortization of goodwill on other than straight-line method if goodwill includes certain intangible factors and if the benefits to be received from the factors decline over the expected life.

— Effective for business combinations initiated on or after March 1, 1976. Application for combinations initiated before March 1, 1976 but consummated on or after that date is encouraged but not required.
No. 10 — Application of FASB Statement No. 12 to Personal Financial Statements, an interpretation of FASB Statement No. 12 (September 1976)

— Specifies that FASB Statement No. 12 applies to personal financial statements of individuals prepared in conformity with generally accepted accounting principles.

— Effective for annual and interim periods ending after October 15, 1976. Early application is encouraged, but retroactive application to previously issued financial statements is not permitted.

No. 11 — Changes in Market Value After the Balance Sheet Date, an interpretation of FASB Statement No. 12 (September 1976)

— When assessing whether a decline in market value below cost is other than temporary, information about a gain or loss realized on subsequent disposition and unrealized gains and losses occurring after the balance sheet date are to be taken into consideration along with other factors. If the decline is other than temporary, the security must be written down to a new cost basis and the loss accounted for as realized. The loss is not to exceed the difference between the market value at the balance sheet date and the asset’s cost.

— Effective for annual and interim periods ending after October 15, 1976. Early application is encouraged, but retroactive application to previously issued financial statements is not permitted.

No. 12 — Accounting for Previously Established Allowance Accounts, an interpretation of FASB Statement No. 12 (September 1976)

— Requires the elimination of temporary allowance accounts for marketable equity securities that were established prior to the effective date of FASB Statement No. 12 and the establishment of a valuation allowance account in accordance with the provisions of FASB Statement No. 12. Any balance remaining in an existing allowance account shall be eliminated by a credit to income in the period in which the Interpretation is initially applied.

— Effective for annual and interim periods ending after October 15, 1976. Early application is encouraged, but retroactive application to previously issued financial statements is not permitted.

No. 13 — Consolidation of a Parent and Its Subsidiaries Having Different Balance Sheet Dates, an interpretation of FASB Statement No. 12 (September 1976)

— Specifies the procedures to be followed and the disclosures required for marketable securities reported in consolidated financial statements that include a parent company and subsidiaries whose fiscal years are different from that of the parent. For example, to compute the amount of any valuation allowance(s) required by FASB Statement No. 12, the aggregate cost and aggregate market value of the portfolio(s) shall be determined for each subsidiary that is consolidated as of the date of each subsidiary’s balance sheet.

- Those aggregates shall then be combined with like figures of the parent determined as of the parent’s balance sheet date. This principle carries through to other aspects of FASB Statement No. 12.

— Effective for annual and interim periods ending after October 15, 1976. Early application is encouraged, but retroactive application to previously issued financial statements is not permitted.

— Stipulates that, when the first condition of paragraph 8 of FASB Statement No. 5 is met with respect to a particular loss contingency and the estimated amount of loss is a range of amounts, the second condition is also met and a loss shall be accrued. If some amount in the range is a better estimate, that amount should be accrued. If no amount is a better estimate of the loss than any other amount, the minimum amount in the range should be accrued. Disclosure is required of the nature of the contingency and the exposure to an additional amount of loss of up to the maximum of the range.

— Effective for annual and interim periods beginning after October 15, 1976. Earlier application is encouraged. An accrual of a loss contingency or an adjustment of an established accrual for a loss contingency resulting from this Interpretation shall be accounted for as a change in estimate in accordance with the requirements of paragraph 31 of APB Opinion No. 20. The Interpretation is not to be applied retroactively to previously issued financial statements.

No. 15 — *Translation of Unamortized Policy Acquisition Costs by a Stock Life Insurance Company*, an interpretation of FASB Statement No. 8 (September 1976)

— Specifies that unamortized policy acquisition costs of a stock life insurance company are to be translated at historical rates.

— Computation of a reserve deficiency shall be made in dollars after translation of the unamortized policy acquisition costs at historical rates and the liability for future policy benefits at the current rate. The computation may require adjustment of a reserve deficiency computed by the foreign subsidiary.

— Effective for all unamortized policy acquisition costs reported in financial statements for annual and interim periods ending after December 15, 1976, except that it shall not be applied prior to initial application of FASB Statement No. 8. If applied concurrently with the initial application of FASB Statement No. 8, it shall be applied in the same manner as FASB Statement No. 8. If FASB Statement No. 8 has been applied prior to adoption of the Interpretation, application of the Interpretation may conform to the manner in which FASB Statement No. 8 was initially applied, or as APB Opinion No. 20 would require.

No. 16 — *Clarification of Definitions and Accounting for Marketable Equity Securities That Become Nonmarketable*, an interpretation of FASB Statement No. 12 (February 1977)

— Clarifies the definition of the terms "marketable" and "restricted stock" and clarifies the requirement of a new cost basis when a marketable security becomes nonmarketable.

— A temporary lack of trades or price quotations for an equity security at the balance sheet date does not make it nonmarketable if the required market prices are available on days closely preceding and following the balance sheet date. The market price of a security shall be determined from sales, bid and ask prices, or quotations, as appropriate, on the first day following the balance sheet date that the information is available.

— A security that is restricted by a governmental or contractual requirement but can reasonably be expected to qualify for sale within one year of the balance sheet date, and for which market price quotations for unrestricted securities of the same class are available as of the balance sheet date, is considered marketable at the balance sheet date.
— When a marketable equity security becomes nonmarketable or a nonmarketable equity security becomes marketable, that security shall be transferred to the appropriate portfolio at cost. The term cost is defined as original cost unless a new cost basis has been assigned based on recognition of impairment of value that was deemed other than temporary or as a result of a transfer from current to noncurrent classification.

— Effective for annual and interim periods ending after March 15, 1977. Earlier application is encouraged, but retroactive application to previously issued financial statements is not permitted.

No. 17 — Applying the Lower of Cost or Market Rule in Translated Financial Statements, an interpretation of FASB Statement No. 8 (February 1977)

— Clarifies the determination of market when applying the rule of cost or market, whichever is lower, in translated financial statements.

— In translated financial statements, translated market shall be current foreign currency replacement cost translated at the current rate, except that:

- Translated market shall not exceed foreign currency net realizable value translated at the current rate; and

- Translated market shall not be less than foreign currency net realizable value reduced by an allowance for an approximately normal profit margin, translated at the current rate.

— Inventory write-downs in translated financial statements shall not be included in the aggregate exchange gain or loss required to be disclosed pursuant to FASB Statement No. 8, but shall be reported in accordance with rules for inventory accounting set forth in Chapter 4 of ARB No. 43.

— Effective for annual and interim periods ending after March 15, 1977. Earlier application is encouraged. Retroactive application is not permitted unless it is applied with an initial application of FASB Statement No. 8.

No. 18 — Accounting for Income Taxes in Interim Periods, an interpretation of APB Opinion No. 28 (March 1977)

— Clarifies the application of APB Opinion No. 28, Interim Financial Reporting, with respect to accounting for income taxes in interim periods.

— The general computation requires the determination of an estimated annual effective tax rate that reflects anticipated investment tax credits, foreign tax rates, percentage depletion, capital gains rates, and other available tax planning alternatives. The rate is to be revised, if necessary, at the end of each successive interim period.

— The effective rate “... shall be applied to the year-to-date ‘ordinary’ income (or loss) at the end of each interim period to compute the year-to-date tax (or benefit) applicable to ‘ordinary’ income (or loss).” The interim-period tax (or benefit) related to “ordinary” income (or loss) shall be the difference between the amount so computed and the amounts reported for the previous interim periods of the fiscal year.
— The interpretation also describes the following:

- Applications to specific situations, for example:
  - "Ordinary" income anticipated for fiscal year
    - Year-to-date income
    - Year-to-date loss
  - "Ordinary" loss anticipated for fiscal year
    - Year-to-date income
    - Year-to-date loss
    - Recognition of the tax benefit of a loss
    - Reversal of net deferred tax credits

- Tax (or benefit) applicable to significant unusual or infrequently occurring items, discontinued operations, extraordinary items, or cumulative effects of changes in accounting principles.

- Special computations applicable to operations taxable in multiple jurisdictions.

- Guidelines for reflecting the effects of new tax legislation.

- Disclosure requirements.

— Effective for financial statements issued after March 31, 1977 for interim periods in fiscal years beginning after December 15, 1976. Earlier application is encouraged, but retroactive application to previously issued financial statements is not permitted.

No. 19 — Lessee Guarantee of the Residual Value of Leased Property, an interpretation of FASB Statement No. 13 (October 1977)

— Deals with the determination of the amount of the lessee's guarantee of the residual value of leased property that should be included in minimum lease payments.

- A lease provision requiring the lessee to make up a residual value deficiency that is attributable to damage, extraordinary wear and tear, or excessive usage does not constitute a lessee guarantee of the residual value.

- If a lease limits the amount of the lessee's obligation to make up a residual value deficiency to an amount less than the stipulated residual value of the leased property at the end of the lease term, the amount of the lessee's guarantee to be included in minimum lease payments under Statement No. 13 shall be limited to the specified maximum deficiency the lessee can be required to make up.

- A guarantee of a residual value amount by an unrelated third party for the benefit of the lessor shall not reduce the amount of the lessee's minimum lease payments unless the lessor explicitly releases the lessee from the obligation to make up the residual value deficiency.

— Effective for leasing transactions and lease agreement revisions entered into on or after January 1, 1978. The provisions of the Interpretation shall be applied retroactively at the same time and in the same manner as the provisions of FASB Statement No. 13 are applied retroactively, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply this Interpretation retroactively.
No. 20 — Reporting Accounting Changes Under AICPA Statements of Position, an interpretation of APB Opinion No. 20 (November 1977)

— An enterprise making a change in accounting principle to conform with the recommendations of an AICPA Statement of Position shall report the change as specified in the statement. If the AICPA statement does not specify the manner of reporting a change, an enterprise making the change shall report the change as specified by APB Opinion No. 20.

— Effective December 1, 1977.

No. 21 — Accounting for Leases in a Business Combination, an interpretation of FASB Statement No. 13 (April 1978)

— Clarifies the application of FASB Statement No. 13, Accounting for Leases, in business combinations.

— The classification of a lease in accordance with the criteria of FASB Statement No. 13 shall not be changed as a result of a business combination unless the provisions of the lease are modified.

- If a lease is modified in connection with a business combination in a way that would result in the revised agreement being designated as new agreement under paragraph 9 of FASB Statement No. 13, then the lease must be classified based on conditions as of the date of the modification of the lease.

— In a pooling of interests, each lease retains its previous classification under FASB Statement No. 13 unless the provisions of the lease are modified as indicated above.

— In a purchase combination, the acquiring enterprise shall retain the previous classification in accordance with FASB Statement No. 13 for the leases of an acquired enterprise unless the lease provisions are modified as indicated above.

- The amounts assigned to individual assets shall be determined in accordance with paragraph 88 of APB Opinion No. 16.

- Subsequent to the recording of the amounts called for by APB Opinion No. 16, leases shall be accounted for in accordance with FASB Statement No. 13.

- Application to leveraged leases is illustrated in Appendix A of the Interpretation.

— Leases acquired in a purchase combination effected prior to the effective date of the Interpretation, shall, on retroactive application of FASB Statement No. 13, be classified as they would have been classified if the acquired enterprise had applied FASB Statement No. 13 retroactively at the date of the business combination.

— Effective for business combinations that are initiated on or after May 1, 1978. The provisions of the Interpretation shall be applied retroactively at the same time and in the same manner as the provisions of FASB Statement No. 13 are applied retroactively.

No. 22 — Applicability of Indefinite Reversal Criteria to Timing Differences, an interpretation of APB Opinions Nos. 11 and 23 (April 1978)

— Specifies that the indefinite reversal concept described in APB Opinion No. 23 is not applicable to areas other than those listed in the Opinion.

- The Interpretation does not modify APB Opinion No. 17 or the AICPA Industry Audit Guide, Audits of Stock Life Insurance Companies.
• Income tax benefits resulting from amortization and depreciation of railroad gradings and tunnel bores for income tax purposes are timing differences requiring comprehensive interperiod tax allocation.

— Effective for timing differences occurring in fiscal years beginning after June 15, 1978 and to be applied prospectively.

No. 23 — *Leases of Certain Property Owned by a Governmental Unit or Authority*, an interpretation of FASB Statement No. 13 (August 1978)

— Clarifies that portion of paragraph 28 of FASB Statement No. 13, *Accounting for Leases*, stating that leases of certain property owned by a governmental unit or authority shall be classified as operating leases.

— Leases of property owned by a governmental unit or authority shall be classified as operating leases only if all of the following conditions are met:
  • Property is owned by governmental unit or authority.
  • Property is part of a larger facility, such as an airport.
  • The property is a permanent structure, or a part thereof.
  • The lessor, or some higher governmental authority, has the explicit right to terminate the lease at any time. Leases of government owned property are not to be classified as operating leases solely because of the lessor’s right of eminent domain.
  • The lease neither transfers ownership nor allows the purchase of the property.
  • The leased property or equivalent property in the same service area cannot be purchased or leased from a nongovernmental unit or authority.

— Leases not meeting all of the above conditions are subject to the same criteria for classification that are applicable to leases not involving government owned property.

— Effective for leasing transactions recorded and lease agreement revisions recorded as of December 1, 1978 or thereafter. The Interpretation shall be applied retroactively at the same time and in the same manner as the provisions of Statement No. 13, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply the Interpretation retroactively.

No. 24 — *Leases Involving Only Part of a Building*, an interpretation of FASB Statement No. 13 (September 1978)

— Clarifies that portion of paragraph 28 of FASB Statement No. 13, *Accounting for Leases*, that states, “when the leased property is part of a larger whole, its cost (or carrying amount) and fair value may not be objectively determinable. . . .”

— If there are no sales of property similar to the leased property, other evidence (such as an independent appraisal of the leased property or estimated replacement cost information) may provide a basis for an objective determination of fair value.

— Effective for leasing transactions recorded and lease agreement revisions recorded as of December 1, 1978 or thereafter. The Interpretation shall be applied retroactively at the same time and in the same manner as the provisions of Statement No. 13, except that enterprises that have already applied Statement No. 13 retroactively in published annual financial statements need not apply the Interpretation retroactively.
No. 25 — Accounting for an Unused Investment Tax Credit, an interpretation of APB Opinions Nos. 2, 4, 11, and 16 (September 1978)

- Clarifies the circumstances, if any, under which an enterprise shall recognize the benefit of an investment tax credit prior to its realization as an offset against federal income tax liability.

- An investment tax credit becoming available in the current period, or carried forward from a prior period, shall be recognized to the extent that the benefit would have been realized if taxes payable had been based on pretax accounting income adjusted for permanent differences.

- Any remaining unused investment tax credit shall be offset against existing net deferred tax credits to the extent of deferred credits that would reverse during the investment tax credit carryforward period, subject to certain limitations.

- The guidelines set forth in APB Opinion No. 11, Accounting for Income Taxes, that permit recognition of net operating loss carryforwards when realization is assured beyond any reasonable doubt do not apply to recognition of unused investment tax credits.

- When the tax benefit of an unused investment tax credit that was recognized is subsequently realized as a reduction of federal income taxes payable, an equivalent amount of deferred tax credits shall be recorded.

- The Interpretation does not apply to companies that recognize the tax benefits of investment credits only to the extent realized as a reduction of federal income taxes payable and defer and amortize those credits over the life of the related property.

- Unused investment credits acquired in a purchase combination shall reduce goodwill recognized in the combination in the period in which the investment credits are realized as an offset to federal income taxes payable. Goodwill (and any amortization thereof) shall not be adjusted retroactively.

- Effective for investment tax credits arising in fiscal years beginning after December 15, 1978 and to be applied prospectively. Unused investment credits arising in earlier years shall be accounted for according to methods presently used.

No. 26 — Accounting for Purchase of a Leased Asset by the Lessee During the Term of the Lease, an interpretation of FASB Statement No. 13 (September 1978)

- Considers whether paragraph 14(c) of FASB Statement No. 13, Accounting for Leases, (which states that "a termination of a capital lease shall be accounted for by removing the asset and obligation, with gain or loss recognized for the difference") is applicable to a termination that results from the purchase of the leased asset by the lessee.

- The termination of a capital lease that results from the purchase of a leased asset is not the type of transaction contemplated by paragraph 14(c) and, therefore, does not give rise to a gain or loss but rather is an integral part of the purchase of the leased asset.

- The purchase shall be accounted for like a renewal or extension of the capital lease. The difference between the purchase price and the present balance of the lease obligation is recorded as an adjustment of the balance of the asset.
— Effective for purchases of leased property recorded as of December 1, 1978 or thereafter. The Interpretation shall be applied retroactively at the same time and in the same manner as the provisions of Statement No. 13, except that enterprises that have already applied Statement No. 13 in published annual financial statements need not apply the Interpretation retroactively.

No. 27 — Accounting for a Loss on a Sublease, an interpretation of FASB Statement No. 13 and APB Opinion No. 30 (November 1978)

— Paragraph 39 of FASB Statement No. 13, Accounting for Leases, does not eliminate the need to recognize a loss on a sublease in those situations in which paragraphs 15-17 of APB Opinion No. 30, Reporting the Results of Operations, require the recognition of the loss.

— If a sublease is entered into as part of a disposal of a segment of a business, as defined in paragraph 13 of APB Opinion No. 30, the anticipated future cash flows that will result from the original lease and the sublease, as well as the carrying amount of any related recorded assets or obligations, shall be taken into account in determining the overall gain or loss on the disposal.

— Effective for estimates of losses at the measurement date (see paragraph 14 of APB Opinion No. 30 for the definition of the measurement date) of a disposal occurring on or after March 1, 1979 and for subleases recorded as of March 1, 1979 or thereafter. Retroactive application is required in accordance with paragraphs 49 and 51 of Statement No. 13.

No. 28 — Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans, an interpretation of APB Opinions Nos. 15 and 25 (December 1978)

— Clarifies when an enterprise shall record compensation expense related to stock appreciation rights and awards under other compensation plans with variable terms (i.e., plans for which the number of shares of stock the employees may receive, the price per share the employees must pay, or both the number of shares and the price are unknown at the date of grant or award) and how the enterprise shall compute that compensation expense.

— Specifies that when stock appreciation rights or other variable plan awards are granted, an enterprise shall measure compensation as the amount by which the quoted market value of the shares covered by the grant exceeds the option price or value specified under the plan, subject to any limitations under the plan.

- Changes in the quoted market value of the shares between the date of grant and the measurement date (the first date on which both (1) the number of shares that an individual employee is entitled to receive, and (2) the option or purchase price, if any, are known) result in a change in the measure of compensation.

— Compensation shall be accrued over the period or periods the employee performs the related services.

- Grants made for past services shall be accrued as a charge to expense of the period in which the rights or awards are granted.

- Up to the measurement date, accrued compensation shall be adjusted in subsequent periods for changes in the quoted market value of the shares, but shall not be adjusted below zero.

- The offsetting adjustment shall be made to compensation expense of the period in which the change occurs.
Guidelines are set forth for accounting for combination plans.

Stock appreciation rights and other variable plan awards are common stock equivalents for purposes of applying the provisions of APB Opinion No. 15, Earnings Per Share, to the extent they are payable in stock.

Effective for stock appreciation rights and other variable plan awards granted in fiscal years beginning after December 15, 1978. The Interpretation shall not be applied retroactively.

- An accrual of compensation expense or an adjustment of accrued compensation resulting from the application of this Interpretation for rights and awards granted in fiscal years beginning before December 16, 1978 shall be accounted for as a change in estimate in the period of change.

No. 29 — Reporting Tax Benefits Realized on Disposition of Investments in Certain Subsidiaries and Other Investees, an interpretation of APB Opinions Nos. 23 and 24 (February 1979)

Clarifies the reporting of income tax benefits realized by an investor from the disposition of an investment in certain subsidiaries and other investees.

An investor shall classify tax benefits realized on disposition of an investment relating to a difference between the accounting basis and the tax basis of the investment in the subsidiary or other investee in the same manner as the classification accorded to gain or loss on disposition of the investment.

- Disclosure shall be made if application of this Interpretation creates a significant variation in the customary relationship between income tax expense and pretax accounting income.

Effective for dispositions occurring after March 1, 1979. Reclassification in previously issued financial statements is permitted but not required.

No. 30 — Accounting for Involuntary Conversions of Nonmonetary Assets to Monetary Assets, an interpretation of APB Opinion No. 29 (September 1979)

Specifies that involuntary conversions of nonmonetary assets to monetary assets are monetary transactions for which gain or loss should be recognized even though an enterprise reinvests or is obligated to reinvest the monetary assets in replacement nonmonetary assets.

- Gain or loss should be recognized in accordance with FASB Statement No. 5, Accounting for Contingencies, if monetary assets are received in a period subsequent to the period when the nonmonetary assets were destroyed or damaged.

- Gain or loss resulting from an involuntary conversion of a nonmonetary asset to monetary assets shall be classified in accordance with the provisions of APB Opinion No. 30, Reporting the Results of Operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions.

- Effective for involuntary conversions of nonmonetary assets to monetary assets occurring in fiscal years beginning after November 15, 1979. Earlier application is encouraged for fiscal years beginning before November 16, 1979 for which financial statements have not been previously issued.

No. 31 — Treatment of Stock Compensation Plans in EPS Computations, an interpretation of APB Opinion No. 15 and a modification of FASB Interpretation No. 28 (February 1980)

Clarifies the provisions of FASB Interpretation No. 28, Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans, that discuss the dilutive effect in EPS computations of stock appreciation rights and other variable plan awards.
— In applying the treasury stock method to stock options, including stock appreciation rights and other variable plan awards, the exercise proceeds of the options are the sum of the amount the employee must pay, the amount of measurable compensation ascribed to future services and not yet charged to expense (whether or not accrued), and the amount of any “windfall” tax benefit to be credited to capital.

- Exercise proceeds shall not include compensation ascribed to past services.

— Provides guidance for computing primary and fully diluted earnings per share.

— Provisions cover EPS treatment of combination plans that allow an employer or employee to choose among various alternative stock option or stock right awards.

— Effective for financial statements for fiscal years beginning after December 15, 1979. Earlier application is encouraged.

- The Interpretation may be, but is not required to be, applied retroactively to previously issued financial statements.

No. 32 — Application of Percentage Limitations in Recognizing Investment Tax Credit, an interpretation of APB Opinions Nos. 2, 4 and 11 (March, 1980)

— Clarifies the application of paragraph 10 of FASB Interpretation No. 25, Accounting for an Unused Investment Tax Credit, with respect to the statutory limitation to be used in recognizing unused investment tax credit.

- The Revenue Act of 1978 changed the statutory percentage limitations that determine the extent to which federal income tax otherwise payable may be offset by investment tax credit.

— The statutory limitations to be used are as follows:

- In the “with-and-without” computation — the statutory percentage limitations in effect for the year the computation is being made, and

- In recognizing investment tax credit in addition to that recognized in the “with-and-without” computation — the statutory percentage limitations applicable to the years in which previously recorded deferred tax credits are expected to reverse.

— In recognizing investment tax credit in addition to that recognized in the “with-and-without” computation the following rules must be observed:

- Only net deferred tax credits that have not been previously offset and that will reverse during the investment tax credit carryforward period, disregarding any timing differences that may originate in that carryforward period, shall be offset by investment tax credit.

- Net deferred tax credits offset by investment tax credit in prior years shall not be adjusted to reflect changes in the statutory percentage limitations.


- Earlier application is encouraged in financial statements for fiscal years beginning before December 16, 1979 that have not been previously issued; however, if the provisions of the Interpretation are adopted early, previously issued financial information for any interim periods of that fiscal year that precede the period of adoption shall be restated.

- The Interpretation shall not be applied retroactively for previously issued annual financial statements.
TECHNICAL BULLETINS ISSUED

79-1 - Purpose and Scope of FASB Technical Bulletins and Procedures for Issuance (December 28, 1979)

- Specifies that the FASB has authorized its staff to issue FASB Technical Bulletins to provide guidance on certain financial accounting and reporting problems on a timely basis.
- Technical Bulletins provide guidance concerning the application of official pronouncements, FASB Statements or Interpretations, APB Opinions, or Accounting Research Bulletins.
  - Technical Bulletins are not Statements or Interpretations to which Rule 203 applies.
  - Technical Bulletins do not establish new financial accounting and reporting standards nor amend existing standards.
  - Technical Bulletins generally address implementation questions heretofore covered by FASB letter communications.
- Technical Bulletins will be used in the following circumstances:
  - The intent of the underlying standard is documented or known to the staff and the answer does no more than clarify, explain, or elaborate upon the underlying standard.
  - The answer is not expected to have a significant effect on either financial reporting in general or most organizations affected by the underlying standard.
  - The administrative cost that may be involved in implementing the answer is not expected to be significant to most affected organizations.
- Technical Bulletins are not approved by the Board, but Board members are informed of all matters proposed for Bulletins and receive copies of all proposed Bulletins prior to issuance.
  - The Director of Research and Technical Activities may expose proposed Technical Bulletins for comment prior to issuance.
- Technical Bulletins are issued in question and answer format.

79-2 - Computer Software Costs (December 28, 1979)

79-3 - Subjective Acceleration Clauses in Long-Term Debt Agreements (December 28, 1979)

79-4 - Segment Reporting of Puerto Rican Operations (December 28, 1979)

79-5 - Meaning of the Term “Customer” as It Applies to Health Care Facilities Under FASB Statement No. 14 (December 28, 1979)

79-6 - Valuation Allowances Following Debt Restructuring (December 28, 1979)

79-7 - Recoveries of a Previous Writedown Under a Troubled Debt Restructuring Involving a Modification of Terms (December 28, 1979)

79-8 - Applicability of FASB Statements 21 and 33 to Certain Brokers and Dealers in Securities (December 28, 1979)
79-9 — Accounting in Interim Periods for Changes in Income Tax Rates (December 28, 1979)

79-10 — Fiscal Funding Clauses in Lease Agreements (December 28, 1979)

79-11 — Effect of a Penalty on the Term of a Lease (December 28, 1979)

79-12 — Interest Rate Used in Calculating the Present Value of Minimum Lease Payments (December 28, 1979)

79-13 — Applicability of FASB Statement No. 13 to Current Value Financial Statements (December 28, 1979)

79-14 — Upward Adjustment of Guaranteed Residual Values (December 28, 1979)

79-15 — Accounting for Loss on a Sublease Not Involving the Disposal of a Segment (December 28, 1979)

79-16 — Effect of a Change in Income Tax Rate on the Accounting for Leveraged Leases (December 28, 1979) (Revised, February 29, 1980)

79-17 — Reporting Cumulative Effect Adjustment from Retroactive Application of FASB Statement No. 13 (December 28, 1979)

79-18 — Transition Requirement of Certain FASB Amendments and Interpretations of FASB Statement No. 13 (December 28, 1979)

79-19 — Investor’s Accounting for Unrealized Losses on Marketable Securities Owned by an Equity Method Investee (December 28, 1979)
EXPOSURE DRAFTS ISSUED AND OUTSTANDING

Proposed Statements of Concepts

Qualitative Characteristics: Criteria for Selecting and Evaluating Financial Accounting and Reporting Policies (August 9, 1979)

— Establishes criteria for selecting and evaluating financial accounting and reporting policies.
  • Policy issues arise whenever alternative accounting or disclosure treatments are possible.
    o Concentrates on the criteria for making accounting and reporting choices, either by the Board or by those who prepare financial reports.
  • The Board anticipates that the criteria set forth will apply to nonbusiness organizations as well as business enterprises.
  • Contains no conclusions about such matters as the identity, number, or form of financial statements or about the unit of measure to be used or attributes to be measured.
  • The present Statement, with the forthcoming Statement on the elements of financial statements of business enterprises, represents the second stage of the structure of the conceptual framework.

— Criteria by which preferred accounting policies may be selected from among available alternatives are set forth in the following hierarchy of qualities:
  • Usefulness for decision making
    o Information’s benefits must exceed its costs.
  • Relevance and Reliability
  • Neutrality, Verifiability, Representational Faithfulness, and Comparability
  • Timeliness, Understandability, Completeness, and Consistency
  • Materiality
— Relevance is that quality of information that renders it capable of making a difference to the decision maker by changing the assessment of the probability of occurrence of some event relating to the attainment of a goal.
  • Degrees of relevance make it possible to trade off some relevance of information for greater reliability.
  • The amount of relevance is specific to the person receiving the information.
  • Information about past events and transactions that has predictive value is relevant.
  • Timeliness is an ancillary aspect of relevance.
    o There may be a trade-off between timeliness and precision.
  • Understandability is an ancillary aspect of relevance.
— Reliability is that quality of information that enables users to depend on it to represent the economic conditions or events that it purports to represent.
  • Two characteristics that are inherent in reliability are verifiability and representational faithfulness.
• Verifiable financial accounting information provides results that would be substantially duplicated by independent measurers using the same measurement methods.
  o Verification implies consensus.
• Representational faithfulness requires that the measure chosen portrays what it purports to portray.
  o Completeness is an ancillary aspect of representational faithfulness and is judged within the bounds of what is material and feasible.
• Reliability does not imply certainty or precision.
• Conservatism deals with uncertainties by avoiding recognition of income on the basis of inadequate evidence and requiring the recognition of losses when assets have been impaired or liabilities incurred.
  – Neutrality requires that accounting information report economic activity as faithfully as possible, without coloring the image it communicates for the purpose of influencing behavior in some particular direction.
  o The criterion of neutrality applies primarily to recognition and measurement rules. It requires freedom from bias.
  o As applied to disclosure standards, neutrality implies evenhandedness as to the different parties at interest.
• Comparability requires that information about an enterprise can be compared with similar information about other enterprises and with similar information about the same enterprise for some other period or point in time.
  o Comparability is not a quality of information as relevance or reliability are, but is rather a quality of the relationship between two or more pieces of information.
  o The purpose of comparison is to detect and explain similarities and differences.
  o In seeking comparability, accountants must not disguise real differences nor create false differences.
  o Consistency is a necessary but not sufficient condition of comparability. Like comparability, consistency is a quality of the relationship between two accounting numbers.
  – Materiality is not a primary characteristic. Its pervasive nature makes it difficult to consider the concept except as it relates to the other qualitative characteristics, especially relevance and reliability.
  o Omission or misstatement of an item in a financial report is material if it is probable that the judgment of a reasonable person relying upon the report would have been changed or influenced by the omission or misstatement.
  o Judgments about materiality in relation to reliability are concerned with errors of measurement.
    o The concept of materiality implies a threshold.
    o General standards of materiality cannot be formulated that would take into account all judgment considerations.
    o Generally, only minimums are specified for quantitative materiality guidelines.
Accounting information must attain some minimum level of relevance and also some minimum level of reliability if it is to be useful.

- A standard-setting body has to meet these needs, but at the same time identify and weigh, however subjectively, the probable immediate costs and benefits to preparers and users and additionally, after the first test, consider the costs and benefits to other parts of the economy.

(Comment period ended November 1, 1979)

*Elements of Financial Statements of Business Enterprises, Revision of Exposure Draft Issued December 29, 1977 (December 28, 1979)*

- Defines eight elements of financial statements of business enterprises that are directly related to measuring performance of an enterprise.

- Definitions are concerned with the essential characteristics of items that qualify as elements.

  - All matters of recognition, measurement, and display have purposely been separated from the definitions of elements
    - To be included in financial statements an item must qualify as an element, but must also meet criteria for recognition and have the relevant attribute capable of reasonably reliable measurement or estimate.
    - Elements of financial statements are accounted for and included in financial statements by the use of accrual accounting procedures. Accrual accounting and related concepts are, therefore, significant not only for defining elements of financial statements but also for understanding and considering other aspects of the conceptual framework for financial accounting and reporting.

- Most of the definitions are expected to apply to organizations other than business enterprises.

- Financial statements of both business enterprises and nonbusiness organizations may have additional elements.

- Elements of financial statements are financial representations of certain enterprise resources, claims to those resources, and the effects of transactions and other events and circumstances that result in changes in those resources and claims.

- The eight elements are of two different kinds or classes:
  - Assets, liabilities, and owners’ equity represent a level or amount at a moment of time.
  - Comprehensive income and its components, revenues expenses, gains, and losses, as well as others, represent the financial effects of transactions and other events and circumstances that affect an enterprise during intervals of time or periods.
  - The relations between the two classes of elements are referred to as “articulation,” that is they result in sets of two or more financial statements that are fundamentally interrelated so that statements that show elements of the first kind depend on statements that show elements of the second kind, and vice versa.
— Assets are probable future economic benefits obtained or controlled by a particular enter-
prise as a result of past transactions or events affecting the enterprise

• An asset has three essential characteristics:
  o A probable future benefit exists involving a capacity, singly or in combination with
    other assets, to contribute directly or indirectly to future net cash inflows.
  o The enterprise can obtain the benefit and control others’ access to it.
    • Legal enforceability of a claim to benefit is not a prerequisite for an asset.
  o The transaction or other event giving rise to the enterprise’s claim to or control of the
    benefit has already occurred.
• Once acquired, an asset continues as an asset until the enterprise collects it, transfers it
  to another entity, or uses it, or another event or circumstance destroys the future ben-
  efit or removes the enterprise’s ability to obtain it.
— Liabilities are probable future sacrifices of economic benefits stemming from present legal,
equitable, or constructive obligations of a particular enterprise to transfer assets or provide
services to other entities in the future as a result of past transactions or events affecting the
enterprise.

• A liability has three essential characteristics:
  o A legal, equitable or constructive duty or responsibility entails satisfaction or settle-
    ment by future transfer or use of assets at a specified event, or on demand.
  o The duty or responsibility obligates a particular enterprise, leaving it little or no dis-
    cretion to avoid the future sacrifice.
    • Legal enforceability is not a prerequisite for an obligation to qualify as a liability.
  o The transaction or other event obligating the enterprise has already happened.
• Once incurred, a liability continues as a liability until the enterprise settles it, or another
  event or circumstance discharges it or removes the enterprise’s responsibility to settle it.
— Owners’ equity is the interest of stockholders or other owners in the assets of an enter-
prise and at any time is the cumulative net result of past transactions and other events and
circumstances affecting the enterprise.

• Owners’ equity is a general interest in an enterprise’s assets, not a claim to specific assets.
— Comprehensive income is the change in owners’ equity (net assets) of an enterprise during
a period from transactions and other events and circumstances from nonowner sources.

• Comprehensive income of an enterprise equals its cash receipts less its cash outlays
  (excluding investment by and distributions to owners) over the life of the enterprise.
• Comprehensive income is the amount by which an enterprise is better or worse off at the
  end of a period than at the beginning as a result of all transactions and other events and
  circumstances affecting it during the period except for investments by and distributions
to owners.
  o Specifically comprehensive income results from:
    • Exchange transactions and other transfers, excluding owners
    • Productive efforts
• Price changes, casualties
• Other effects of interaction between an enterprise and its total environment

• Comprehensive income, as defined, is a return on financial capital as distinguished from a return on physical capital.
  o The essential difference in the two concepts is that "holding gains and losses" are included in income under the financial capital concept, but are treated as "capital maintenance adjustments" under the physical capital concept.
  o The term "earnings" has not been used because it may be used to designate a different concept that is a component part of comprehensive income, and it may be based on either a return on physical capital or on financial capital.
• Capital maintenance concepts are the subject of another project.
• The Board has not as yet chosen between the financial and physical capital maintenance concepts for deciding the meaning and appropriate display of "earnings."

• Comprehensive income comprises two related but distinguishable types of components:
  o Revenues, expenses, gains and losses
  o Intermediate components or measures such as gross margin, contribution margin, earnings from continuing operations, and the like
• The definitions do not prejudge how information about comprehensive income and its components should be displayed, nor do they designate a "bottom line" for any statement.

— Revenues are inflows or other enhancements of assets of an enterprise or settlements of its liabilities (or a combination of both) during a period from delivering or producing goods, rendering services, or other activities that constitute the enterprise's ongoing major or central operations.
• Revenues represent actual or expected cash inflows that have occurred or will eventuate as a result of the enterprise's ongoing major or central operations during the period.
— Expenses are outflows or other using up of assets or incurrences of liabilities (or a combination of both) during a period from delivering or producing goods, rendering services, or carrying out other activities that constitute the enterprise's ongoing major or central operations.
• Expenses represent actual or expected cash outflows that have occurred or will eventuate as a result of the enterprise's ongoing major or central operations during the period.
— Gains (or other appropriately descriptive terms) are increases in owners' equity (net assets) from peripheral or incidental transactions of an enterprise and from all other transactions and other events and circumstances affecting the enterprise during a period except those that result from revenues or investments in the enterprise by owners.
— Losses (or other appropriately descriptive terms) are decreases in owners' equity (net assets) from peripheral or incidental transactions of an enterprise and from all other transactions and other events and circumstances affecting the enterprise during a period except those that result from expenses or distributions by the enterprise to owners.
Elements of financial statements are accounted for and included in financial statements by the use of accrual accounting procedures. Accrual accounting and related concepts include the following processes:

- Accrual is the accounting process of recognizing noncash events and circumstances as they occur; specifically, accrual entails recognizing revenues and related increases in assets and expenses and related increases in liabilities for amounts expected to be received or paid, usually in cash, in the future.

- Deferral is the accounting process of recognizing a liability for a current cash receipt or an asset for a current cash payment (or current incurrence of a liability) with an expected future impact on revenues or expenses.

- Allocation is the accounting process of assigning or distributing an amount according to a plan or a formula. It is a broader term than amortization — that is, amortization is an allocation process.

- Amortization is the accounting process of systematically reducing an amount by periodic payments or write-downs.

- Realization is the process of converting noncash resources and rights into money and is most precisely used in accounting and financial reporting to refer to sales of assets for cash or claims to cash. The related terms, realized and unrealized, therefore identify revenues or gains or losses on assets sold and unsold, respectively.

- Recognition is the process of formally recording or incorporating an item in the accounts and financial statements of an enterprise. Thus, an element may be recognized (recorded) or unrecognized (unrecorded). "Realization" and "recognition" are not used as synonyms, as they sometimes are in accounting and financial literature.

The Board emphasizes that the definitions in this Statement neither require nor presage upheavals in present practice, although they may in time lead to some changes in practice or at least in the ways some items are viewed.

- Contrary to conclusions reached by some respondents to the Discussion Memorandum and earlier Exposure Draft, all or most deferrals of costs are not precluded by the definition of assets, and all or most "deferred credits" and "reserves" are not precluded by the definition of liabilities.

- The one exception noted in the Exposure Draft is that under the definitions of elements both the liability method and the net-of-tax method are compatible with the Statement. The deferred method, prescribed by APB Opinion No. 11 *Accounting for Income Taxes*, does not fit the definitions.

(Comment period ends May 15, 1980)

**Objectives of Financial Reporting by Nonbusiness Organizations (March 14, 1980)**

- The proposed Statement establishes the objectives of general purpose external financial reporting by nonbusiness organizations.

- The major distinguishing characteristics of nonbusiness organizations include:
  - Receipts of a significant amount of resources from providers who do not expect repayment or benefits proportionate to resources provided.
  - Operating purposes that are primarily other than profit or profit-equivalent oriented.
  - Absence of defined ownership interests that can be sold, transferred, or redeemed, or that convey a share of resources on liquidation of the organization.
Organizations included in this Statement are:

- Private nonprofit and philanthropic organizations.
- State and local governmental units.
  - The Board is not assuming responsibility for setting state and local government accounting standards by publishing the Exposure Draft.
- Membership organizations.

General purpose external financial reporting focuses on meeting the information needs of external users who cannot prescribe the information they want.

- External users include members, taxpayers, contributors and creditors.

Financial reporting comprehends financial statements, and extends to other means of communicating information about an organization's resources and obligations.

- Financial reporting by nonbusiness organizations is limited in its ability to provide direct measures of the quality of goods and services provided in the absence of market-determined exchange prices, or the degree to which they satisfy the needs of service beneficiaries and other consumers.
- The information provided by financial reporting largely reflects the effects of transactions and events that have already happened.

The objectives of financial reporting for nonbusiness organizations are to provide information useful to present and potential resource providers for:

- Making rational decisions about the allocation of their resources to those organizations.
- Assessing the services that a nonbusiness organization provides and its ability to continue to provide those services.
  - Information on the relation of services provided to resources used enables resource providers to assess the performance of the organization.
- Assessing management's discharge of its stewardship responsibilities.
  - Managers are also accountable for compliance with statutory, contractual, or other limitations.
  - Financial reporting, and especially financial statements, does not separate managers' performance from an organization's performance.

Financial reporting should provide the following information about an organization:

- Economic resources, obligations and net resources.
  - This information should provide direct indications of the cash flow potential of some resources and the cash needed to satisfy obligations.
  - Restrictions on the use of resources must be identified. Restrictions control the types and level of services an organization is able to provide.
- Organization performance, which includes:
  - Periodic measurement of the changes in the amount and nature of the net resources.
  - Information on the service efforts and accomplishments of the organization.
    - Measurement of service efforts and accomplishments may be outside the scope of financial reporting.
• Information about service efforts and accomplishments may include information quantified either in units of survey or in units other than money and nonquantified information.

• Nature and relation between resources inflows and outflows. A distinction should be drawn between inflows that change net resources, and those that do not do so.

• Organization performance and resource inflows and outflows should be based on the accrued method of accounting.

• Cash flows.

• Explanations and interpretations.

— The objectives lead to, but leave unanswered, questions such as the identity, number, and form of financial statements; elements of financial statements, including recognition, measurement, and display; and criteria for determining the reporting entity.

(Comment period ends September 15, 1980)

**Proposed Statements of Standards**

*Lessee's Use of the Interest Rate Implicit in the Lease*, an amendment of FASB Statement No. 13 (November 6, 1978)

— Specifies the interest rate that a lessee shall use to compute the present value of the minimum lease payments to determine whether a lease should be classified as a capital lease under paragraph 7(d) of FASB Statement No. 13, *Accounting for Leases*.

(Comment period ended January 5, 1979)

(The Board decided, on December 12, 1979, not to issue a Statement.)

*Estimates of Residual Values by Lessors and Lessees*, an amendment of FASB Statement No. 13 (May 10, 1979)

— Specifies that the determination of estimated residual value of leased property as at the end of the lease term shall be made in the light of price levels and market conditions prevailing at the inception of the lease without consideration of potential increases in value due to changes in future price levels or market values.

(Comment period ended July 13, 1979)

(The Board decided, on December 12, 1979, not to issue a Statement.)

**Interim Special Industry Reports on FASB Statement No. 33, Financial Reporting and Changing Prices** (May 31, 1979 and June 12, 1979)

— The FASB established six industry task groups to deal with the unique problems of implementing the specific proposals on accounting for the effects of inflation. The six industries are:

- Banking (including thrift institutions)
- Forest Products
- Insurance
- Mining
Disclosure of Pension and Other Post-Retirement Benefit Information, an amendment of APB Opinion No. 8 (July 12, 1979)

— Modifies the disclosure rules of APB Opinion No. 8, Accounting for the Cost of Pension Plans, requiring an employer having only one defined benefit pension plan to make the following disclosures as of the most recent date in the current fiscal year on which the actuarial present value of accumulated plan benefits has been determined:

- The actuarial present value of accumulated plan benefits.
- The actuarial present value of vested plan benefits.
- The plan’s net assets available for benefits.
- Disclosures of such details as actuarial assumptions and asset valuation methods.

All of the above are to be determined in accordance with the revised Pension Plan Exposure Draft.

- An employer that has more than one ongoing defined benefit pension plan shall make the disclosures detailed above separately for each of the following two groups:
  - Plans that have an actuarial present value of accumulated plan benefits in excess of net assets available for those benefits.
  - Plans that have net assets available for benefits in excess of the actuarial present value of accumulated plan benefits.

- Exceptions are provided for certain multiemployer plans and for plans with fewer than 100 participants.

- Disclosure requirements also cover other post-retirement benefits.

- Does not focus on the issue of what is the appropriate measure of the employer’s cost and obligation with respect to pension benefits. This subject is part of a separate project on accounting by employers for pensions.

- Would be effective for annual financial statements for fiscal years beginning after December 15, 1979. The disclosures need not be included in financial statements for periods beginning before the effective date.

(Comment period ended September 21, 1979)

Accounting for Compensated Absences (December 17, 1979)

— Considers the accounting by employers for compensation costs of absences from employment for vacation, holiday, illness, or other personal activities for which it is expected that an employee will be paid.

- Current accounting practice either accrues these costs over some period of time before payment, or recognizes the costs at the time of payment.

- The Board concluded that for each accounting period, employers shall accrue the liability for compensated absences for estimated probable future payments attributable to employees’ service during that period.
— Would be effective for fiscal years beginning after December 15, 1979 and interim periods within those fiscal years.

- Accounting changes adopted to conform to the provisions of this Statement shall be applied as follows:
  - If the effect of the changes is material to the net income of any period presented, those changes shall be applied retroactively.
  - If the effect of those changes is not material to the net income of any period presented, those changes shall be applied by a cumulative adjustment to opening retained earnings of the earliest period presented and such adjustment shall be disclosed.

(Comment period ended February 18, 1980)

Accounting for Preacquisition Contingencies of Purchased Enterprises, an amendment of APB Opinion No. 16 (December 26, 1979)

— Specifies the application of FASB Statement No. 5, Accounting for Contingencies, FASB Statement No. 16, Prior Period Adjustments, and APB Opinion No. 16, Business Combinations, to preacquisition contingencies of purchased enterprises and adjustments that result from resolution of those contingencies.

— Requires that during the “allocation period” (defined below), contingent assets, contingent liabilities, and contingent impairments of assets shall be recorded as a part of the allocation of the cost of the acquired enterprise if they meet the following criteria:

- Information available prior to the end of the “allocation period” indicates that it is probable that an asset existed, a liability has been incurred, or an asset had been impaired at the consummation of the business combination. It is implicit in this condition that it is probable that one or more future events will occur confirming the fact of the asset, liability, or impairment.
- The amount of the asset, liability, or impairment can be reasonably estimated.

— “Allocation period” is defined as the period that is required to identify and quantify the assets acquired and the liabilities assumed.

- The “allocation period” ends when the acquiring enterprise is no longer waiting for information that it has arranged to obtain and that is known to be available or obtainable.
- The existence of a preacquisition contingency for which an asset, a liability, or an impairment of an asset cannot be estimated does not, of itself, extend the “allocation period.”
- The allocation period will usually not exceed one year from the consummation of the business combination.

— After the end of the “allocation period,” adjustments that result from preacquisition contingencies, other than adjustments that result from realized income tax benefits of preacquisition operating loss carryforwards, shall be included in the determination of net income in the period in which the adjustments are recognized.

— Would be effective for adjustments that are determined in fiscal years beginning after June 15, 1980.

- Earlier application to statements not previously issued is encouraged but not required.
• The Statement shall not be applied retroactively to previously issued financial statements, except in cases where the initial recording of a preacquisition contingency was not in accordance with the Statement and that contingency has not been resolved prior to the effective date of this Statement. In that case it may be applied retroactively.

(Comment period ended February 29, 1980)

**Balance Sheet Classification of Deferred Income Taxes, an amendment of APB Opinion No. 11 (March 14, 1980)**

— Clarifies the classification of deferred income tax charges and credits when there is no asset or liability in the balance sheet related to the timing difference.

— A deferred charge or credit that is related to an asset or liability shall be classified as current or noncurrent based on the classification of the related asset or liability.

— A deferred charge or credit that is not related to an asset or liability shall be classified based on the expected reversal date of the specific timing difference, applying the same criteria used for classifying other assets and liabilities.

• A deferred charge or credit is not related to an asset or liability if:
  o There is no associated asset or liability.
    • A change in accounting method for tax purposes, as for example from the cash method to the reserve method of accounting for bad debts, the effect being amortized for tax purposes over ten years, would give rise to a deferred tax item unrelated to trade receivables or provisions for doubtful accounts. The collection or write-off of the receivables will not cause the timing differences to reverse. The timing difference will reverse over time.
    o A reduction of an associated asset or liability will not cause the timing difference to reverse.
      • The term "reduction" includes amortization, sale or other realization of an asset and amortization, payment or other satisfaction of a liability.

— Would be effective for financial statements for periods ending after December 16, 1980. Earlier application is encouraged.

• Reclassification in previously issued financial statements is permitted but not required.

(Comment period ends May 14, 1980)

**Proposed Interpretations**

*Reporting Intercorporate Income Tax Allocations, an interpretation of APB Opinions No. 11 and 22 (August 20, 1979)*

— Specifies that the disclosures required by APB Opinion No. 22, *Disclosure of Accounting Policies*, apply to the separate financial statements of a parent company or a subsidiary that joins in the filing of a consolidated income tax return.

(Comment period ended October 19, 1979)

(The Board decided not to issue an Interpretation at this time, and remanded it back to the AICPA for possible specific emerging problems.)
Applicability of APB Opinion No. 21 to Television Film License Agreements, an interpretation of APB Opinion No. 21 (September 28, 1979)

— Concludes that APB Opinion No. 21, Interest on Receivables and Payables, applies to receivables and payables arising from television film license agreements.
  
  • Interest should be imputed if such agreements have terms that exceed approximately one year and have either no stated interest rate or a stated interest rate that varies from prevailing interest rates.

— Would be effective upon issuance. Application would be retroactive by restating the financial statements of prior periods.

  (Comment period ended November 30, 1979)

  (The Board decided on January 23, 1980 to defer action until later when the matter will be considered with the specialized accounting principles and practices.)

Applying FASB Statement No. 34 to Oil and Gas Producing Operations Accounted by the Full Cost Method, an interpretation of FASB Statement No. 34 (January 28, 1980)

— Specifies that for purposes of applying Statement No. 34, Capitalization of Interest Cost, to oil and gas operations accounted for by the full cost method, assets in use in the earnings activities of the enterprise do not qualify as assets as defined in paragraph 9 of Statement No. 34 for capitalization of interest cost.

  • Assets in use in earnings activities include assets whose costs are being currently depreciated, depleted, or amortized.

— Unusually significant investments in unproved properties and major development projects that are not being currently depreciated, depleted, or amortized and on which exploration or development activities are in progress are qualifying assets for capitalization of interest cost.

— Would be effective upon issuance. The provisions of this Interpretation are to be applied at the same time as the provisions of Statement No. 34 are first applied.

  (Comment period ends March 28, 1980)
DISCUSSION MEMORANDA ISSUED—For which Exposure Drafts have not been issued to date

Concepts


— The Board’s project on a conceptual framework for financial accounting and reporting is a major, continuing project that is being carried out in several phases:

- Definition and measurement of the elements of financial statements. An Exposure Draft was issued on definition of the elements of financial statements on December 29, 1977 and a revised Exposure Draft on the subject of elements was issued on December 28, 1979.
- Form and content of financial statements.
- Allocation of costs and certain aspects of revenue recognition.

— The Discussion Memorandum contains no conclusions of the Board. The Memorandum is divided into three parts:

- Defining the elements of financial statements (Part I).
- Identifying the qualitative characteristics of financial information (Part II).
- Selecting the attributes of the elements that should be measured (Part III).

— The conceptual framework is to be a constitution, a coherent system of interrelated objectives and fundamentals that can lead to consistent standards and that prescribe the nature, function, and limits of financial accounting and financial reporting.

— Part I relates to the definition of the elements of financial statements. One of the critical issues is the conceptual view of earnings. Two principal conceptual views of earnings are advanced:

- The asset and liability view, under which earnings are determined as a measure of the change in net economic resources.
- The revenue and expense view, which focuses on the matching process and on revenue and expense measurement.

  (An Exposure Draft on Part I was re-issued by the Board on December 28, 1979.)

— Part II concentrates on the qualitative characteristics of financial information. Of special concern is how qualities that are already widely accepted can become effective criteria or standards. (An Exposure Draft on Part II was issued by the Board on August 9, 1979.)

— Part III deals with the measurement of the elements of financial statements and focuses on the selection of the attribute of those elements that is to be measured and the selection of the unit of measurement.

  (FASB Statement No. 33, *Financial Reporting and Changing Prices*, is considered by the Board to be a phase of the measurement project.)
The Board has concluded that a separate class of pronouncements will be issued to avoid the problems that would arise if the regular series of FASB Statements were used. The principal reason relates to Rule 203 of the Code of Professional Ethics of the AICPA, which makes FASB Statements binding on members, with noncompliance by an audit client calling for a qualification in the auditor's report. If conceptual pronouncements were issued under the aegis of Rule 203, the operation of the rule might cause significant and undesirable disruptions in financial reporting.

Criteria for Determining Materiality (Issued March 1975, public hearing held May 20, 1976) (The project has been combined with the Qualitative Characteristics project.)

The objective of the Board is to establish materiality criteria which, when applied, will result in consistent financial reporting of matters necessary for an understanding of an enterprise's financial activities. Such criteria should be capable of practical application to various types of items in varying circumstances.

The scope of this project is limited to consideration of criteria for determining materiality applicable only to the general purpose financial statements of profit-oriented enterprises.

Focus is on materiality in financial accounting and reporting. However, the results of the project may be useful in any consideration of materiality in auditing.

The Discussion Memorandum is developed along two major lines of inquiry:

- To provide users an overview of the complexities of the accounting and reporting process and of the resulting practical difficulties confronting those who make decisions involving the determination of materiality, and
- To provide preparers and auditors with an overview of the needs and expectations of the primary users of financial statements.

The basic issues set forth in the Discussion Memorandum focus on the orientation and frame of reference, and the level of specificity of criteria for determining materiality as well as the mode of expression of the criteria—for example, quantitative, qualitative or some combination of the two. Implementation issues are set forth to elicit comments helpful in developing specific criteria.

Reporting Earnings (Issued July 31, 1979, public hearings held on December 3 and 4, 1979)

The project on reporting earnings focuses mainly on questions of disclosure. It raises issues concerning disclosure of components of earnings not now displayed, and the exclusion of some components of earnings from the computation of net earnings for the current year.

- The main purpose of the Discussion Memorandum is to consider whether the benefits of additional disclosures may exceed the associated costs.
- The project overlaps two other projects of the Board:
  - Financial Statements/Financial Reporting
  - Reporting Funds Flow and Liquidity
- The concept of earnings used in this project is the increase in net assets or owners' equity from all transactions and other events and circumstances affecting the enterprise during the period, excluding the effects of certain transactions with owners.
The applicability of the conclusions of FASB Statement of Financial Accounting Concepts No. 1, *Objectives of Financial Reporting by Business Enterprises*, to the reporting of information on earnings is discussed to derive criteria for deciding which reporting alternatives are to be preferred.

- Specific attention is devoted to various user needs, such as:
  - Assessing the volume of regular activities and the revenues generated by those activities.
  - Assessing earnings from regular activities, which requires the assessment of regular expenses.
  - Information about irregular revenues, expenses, gains, and losses.

- Additional consideration is given to the form of presentation and to summary indicators and ratios, such as earnings-per-share information and rates on capital employed.

- The nine specific issues raised in the Discussion Memorandum deal with such matters as:
  - The detail in which volume of activity and regular revenues is to be reported.
  - The manner of reporting regular expenses; for example, as fixed and variable, or in functional categories.
  - The criteria to be used for identifying irregular revenues, expenses, gains and losses.
  - Single-step versus multiple-step income statements.
  - The exclusion of any components of earnings from the earnings statement for the current period, and inclusion of them in a separate statement or as a direct adjustment to equity interest.
  - The presentation of a five-year summary of earnings.

- Two advisory issues included in the Discussion Memorandum deal with certain aspects of cash flow reporting and the reporting of an earnings forecast.

**Standards**

*Accounting for Research and Development and Similar Costs* (Issued December 28, 1973, public hearing held on March 15, 1974)

- The parts dealing with research and development costs have resulted in FASB Statement No. 2.
- The parts dealing with development stage companies have been dealt with in FASB Statement No. 7.
- The parts dealing with "Similar Costs" have not yet resulted in any action by the FASB. These deal primarily with preoperating and plant start-up costs, market research, product promotion costs, plant relocations, assembly-line rearrangements, hotel and store opening costs, and other costs (such as insurance acquisition costs). The Board announced that it has no plans at this time for further deliberations on costs similar to R&D. Such consideration is to await completion of the development of a conceptual framework for accounting and reporting.
Accounting for Business Combinations and Purchased Intangibles (Issued August 19, 1976; the public hearing originally scheduled for May, 1977 was cancelled and will be rescheduled some time after the issuance of a Statement on elements of financial statements of business enterprises)

— The objective of this project is to determine appropriate financial accounting and reporting standards for business combinations and purchased intangibles within the existing framework of historical-cost financial statements.

— The memorandum is divided into three levels.

— The first level deals with basic and implemental issues involving choices about alternative procedures for giving effect to conceptual decisions, including such basic issues as:
  • How should the identifiable assets and liabilities of the constituent companies be accounted for in the combined enterprise’s financial statements?
  • How should positive goodwill be accounted for in a combination?
  • How should the excess of the current value of a constituent company’s net identifiable assets over the aggregate cost for that company be accounted for?
  • How should purchased intangibles be accounted for?

A series of implementation issues surrounds these basic issues.

— The second level of the memorandum addresses technical issues or aspects of applying accounting standards to specific business combinations, including such matters as income tax accounting, treatment of contingent consideration, treatment of accounting changes, etc.

— The third level of the memorandum includes ten appendices that provide background or detailed information related to various issues.

Interim Financial Accounting and Reporting (Issued May 25, 1978, public hearing held on September 26, 1978) Project is inactive. Future work will be determined after the issuance of a Statement on elements of financial statements of business enterprises.

— The central objective of this project is to determine appropriate accounting and reporting standards for financial statements and summarized financial data covering periods shorter than a year.

— The scope of the project embraces all issues considered in APB Opinion No. 28, Interim Financial Reporting, FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements, and FASB Interpretation No. 18, Accounting for Income Taxes in Interim Periods, and other relevant issues such as interim period segment information disclosure and prior period adjustments.

• Any resulting Statement would not modify accounting standards for an annual period.

• Measurement alternatives to be considered are limited to those found under the present accounting model.

• The project will not modify the provisions of the Addendum to APB Opinion No. 2, Accounting for the “Investment Credit,” but additional disclosures may be required of covered industries.
The Discussion Memorandum addresses eight basic issues:

- The objectives, uses, elements, and qualitative characteristics of interim financial reports versus those of annual reports.
- Interim period expense recognition and measurement.
  - Interim period viewed as an integral part of an annual period.
  - Interim period viewed as a discrete segment of history.
  - Adoption of both integral and discrete viewpoints, with selective application to different types of transactions or events.
- Determination of interim inventory under LIFO.
- Basis of provision for estimated interim period income taxes.
  - Estimated effective tax rate for the year.
  - Income tax expense applicable to interim period income.
  - Some combination of the two methods.
- Treatment of prior period adjustments.
- Interim period disclosure requirements.
- Applicability of interim period reporting requirements to different business enterprises; for example, all enterprises, only publicly held enterprises, etc.
- Application of a standard on a retroactive or prospective basis.

Effect of Rate Regulation on Accounting for Regulated Enterprises (Issued December 31, 1979; public hearings May 28 and 29, 1980)

- The Discussion Memorandum focuses on the effect of rate regulation on financial accounting and reporting for enterprises whose prices are regulated by governmental agencies.
  - Although the primary emphasis is on public utilities and health care organizations, consideration is also given to other regulated industries such as airlines, motor carriers, railroads, and insurance.
  - Rate regulated industries are classified by type of regulation:
    - Individual cost of service — public utilities
    - Group rate setting — airlines, insurance, motor carriers, and railroads
    - Combination of individual cost of service and group rate setting — health care organizations
- The objectives of this project are threefold:
  - To determine whether there are circumstances that would support a different application of generally accepted accounting principles by regulated enterprises in general-purpose financial statements than is applied by nonregulated enterprises.
  - To identify any such circumstances, principally resulting from rate making, and to determine any impact they should have on the identification and measurement of assets, liabilities, revenues, and expenses.
  - To establish criteria for recognizing when circumstances exist that should be reflected in the application of generally accepted accounting principles by regulated enterprises.
Impetus for the study came from the SEC and the AICPA’s Accounting Standards Division.

- The SEC requested the FASB to reconsider the Addendum, “Accounting Principles for Regulated Industries,” to APB Opinion No. 2, Accounting for the “Investment Credit.”
  - The Commission noted problems with the Addendum, such as confusion over the applicability of FASB Statement No. 13, Accounting for Leases, to rate-regulated enterprises, and, in general, defining what is not a rate-regulated enterprise.
- The AICPA’s concern stemmed from the variety of interpretations in practice of the Addendum, and the increasing difficulty of identifying the industries to which the Addendum should apply.

The Discussion Memorandum includes eleven key issues and twenty-six subissues.

- The threshold issue, to which an affirmative answer would render the remaining issues largely irrelevant, is, “Should accounting prescribed by regulatory authorities be considered in and of itself generally accepted for purposes of financial reporting by rate-regulated enterprises?”
- The remaining ten key issues deal with such questions as:
  - Does rate regulation, or only specific types of rate regulation, introduce an economic dimension that should affect the application of generally accepted accounting principles?
  - Should any pronouncement on this subject issued by the Board identify specific industries affected, or should the pronouncement deal with concepts and criteria for application?
  - Should the financial statements of a regulated enterprise disclose the effect of differences between those statements and what they would be if the enterprise were non-regulated?
  - How should any new standards on accounting for the impact of rate regulation be applied?

INVITATIONS TO COMMENT

Evaluation of FASB Statements in Effect at Least Two Years (Issued May 31, 1978)

- Invites written comments from financial statement preparers, auditors, users and others about their experiences in applying FASB Statements Nos. 1-12 and in using the resulting financial information.
- Comments are invited, particularly on FASB Statement No. 5, Accounting for Contingencies, and FASB Statement No. 8, Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements. (The Board has agreed to reconsider the conclusions of FASB Statement No. 8 and has placed the matter on its technical agenda.)
- Comments on APB Opinions and Accounting Research Bulletins also are requested.
- Respondents are asked to state specific reasons for recommending re-examination of a pronouncement, and to set forth specific proposals for solution together with supporting reasoning. Proposals should include comments on:
  - The effect of the proposal on financial reporting of all classes of enterprises in all types of industries affected by a particular Statement.
• Consistency of the proposal with the requirements of other existing pronouncements.
• The possibility that further progress in the Conceptual Framework project will significantly affect the proposal.

(Comment period ended August 15, 1978)

Note: In response to comments received, the Board has added to its agenda a reconsideration of FASB Statement No. 8; deferred reconsideration of FASB Statement No. 5; and declined to reconsider ARBs Nos. 43 and 51, APB Opinions Nos. 4, 6, 9, 11, 15, 18, 19, 20, 21, 25, 26 and 30, FASB Statements Nos. 2, 3, 4, 6, 7, 9, 10, 11, 12 and 22 and FASB Interpretations Nos. 18 and 22 at this time.

RESEARCH REPORTS ISSUED

Field Tests of Financial Reporting in Units of General Purchasing Power (May 1977)


— The study identifies and defines the issues of financial accounting in nonbusiness organizations, and is intended to assist the FASB to evaluate whether it is feasible and desirable for it to become involved in specific projects in this area.

— The study is organized to raise substantive issues and to give arguments, pro and con, with no attempt to resolve the issues. It covers the following topics:
  • It explores the current state of financial accounting and reporting by nonbusiness organizations.
  • It attempts to identify the users of external financial statements of nonbusiness organizations and their information needs.
  • It relates those user needs to information supplied by different types of financial statements.
  • It explores certain specific financial accounting and reporting areas that are controversial and nonuniform, such as pensions and depreciation.
  • It concludes by exploring the appropriate boundaries for a set of accounting concepts for nonbusiness organizations, including the question of whether separate accounting concepts are needed for nonbusiness organizations, and whether separate concepts may be needed for the governmental, nongovernmental, or other categories of the nonbusiness spectrum.

— The Board expects in the near future to solicit formal responses, and to announce dates and places for public hearings on the issues.

Economic Consequences of Financial Accounting Standards—Selected Papers (July 1978)


• Research on economic consequences of financial accounting standards is being encouraged by the FASB to gain a better understanding of the following factors:
  ◦ The types of economic consequences that accounting standards can have.
The processes by which "side effects" occur.

The nature and accuracy of the techniques available for measuring and predicting such "side effects."

Six independent research studies are published in the Research Report.

- "Accounting Changes in Principles and Estimates, How Different Are They?" by W.T. Harrison, Jr.


- The purpose of the report is to examine the impact of FASB Statement No. 5, Accounting for Contingencies, on the practice of corporate risk and insurance management—in particular, to determine if that Statement has caused enterprises to make unsound risk and insurance management decisions.

- Several hypotheses were tested by comparing a study group of 74 enterprises that had self-insurance reserves in the two years before Statement No. 5 was issued with a control group of 85 enterprises that had not established self-insurance reserves before the issuance of the Statement.

- The main hypotheses tested were that Statement No. 5 encouraged enterprises to make economically unjustified decisions to purchase insurance or reinsurance, to increase coverage on insured exposures, to spend more for legal, loss protection and loss prevention services, and to alter insurance and reinsurance contracts between subsidiary insurance companies and their parent companies.

- The study revealed no significant differences between the risk management decisions of enterprises that had self-insurance reserves before Statement No. 5 was issued and those of enterprises that had not established self-insurance reserves before the issuance of the Statement.


- Attempts to evaluate the economic impact of FASB Statement No. 8, Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements on the foreign exchange risk management (FERM) practices of U.S. multinational corporations.

- A mail-survey technique was used as the principal method of acquiring the data upon which the results of the study are based.
— Evaluation of the impact on FERM of FASB Statement No. 8 essentially is based on a comparison of data collected in an earlier research survey, conducted in 1975, on the FERM practices of companies with the practices of those same companies and additional companies following the issuance of Statement No. 8.

• Adjustments were made to reflect expected changes in FERM resulting from the normal growth in the volume of international business of the firms which responded to the survey.

— Some of the conclusions reached by the study are:

• Firms whose accounting practices did not conform closely to Statement No. 8 when it was issued are pursuing more aggressive FERM programs. Therefore, Statement No. 8 did have an impact on the way that firms manage foreign exchange.

• Statement No. 8 has had an impact on investment policies.
  o Some firms have refrained from making foreign investments. Others have adjusted their “hurdle rate” due to exchange risk.
  o Dividend payments from subsidiaries in weak currency countries have been accelerated by some companies to reduce their exposure.

• A major question that remains unresolved from the data made available is whether the increased level of resources devoted to the exchange risk management function has generated a significant increase in the after-tax cash flow of the multinational corporation.


— The objective of the research study is to investigate whether, in general, the common stock security returns of multinational firms were significantly affected by the issuance and implementation of FASB Statement No. 8, Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements.

• Common stock security returns are defined as the change in share prices between the beginning and end of a period plus dividends received during that period, all divided by the common stock share price at the beginning of the period (adjusted for stock splits and stock dividends, where necessary).

— The study investigates the securities market behavior of firms affected by FASB Statement No. 8 both prior and subsequent to its issuance. The report discusses the research effort, provides a summary of the findings, and considers the limitations and issues yet to be addressed.

— The major finding of the study is that the issuance and implementation of FASB Statement No. 8 does not appear to have had significant detectable effects on the security returns of multinational firms.


— Concludes that the issuance of FASB Statement No. 19, Financial Accounting and Reporting by Oil and Gas Producing Companies, had no significant impact on the stock prices of oil and gas producing companies using full cost accounting relative to those using the successful efforts method.
Tests were conducted on oil and gas producing firms affected by the Statement by comparing the security return behavior (change in stock prices plus dividends) of the affected full cost firms with that of successful efforts firms for several weeks before and after the date of issuance of that document.

PROCEEDINGS ISSUED

- Financial Reporting and Changing Prices—The Conference, Paul A. Griffin, Editor (June 1979)
  
  * Includes papers and special industry reports presented at an FASB Conference on Financial Reporting and Changing Prices held May 31, 1979 in New York City.

  * The Conference dealt with the following aspects of financial reporting and changing prices:
    
    o Its public importance
    o Effects on management decisions and actions
    o Impact on decisions by investors, creditors, and others
    o Perspective of the Securities and Exchange Commission
    o Implication for certain industries

BACKGROUND PAPERS ISSUED

- Accounting for Pensions by Employers (March 1980)
  
  * The major concern of the FASB project on accounting by employers for pensions and other retirement benefits is the determination of periodic cost and liability, if any, to be recognized by employers.

  * The two types of pension plans identified are:

    o Defined benefit plans (plans that state the basis for determining the pension benefits retirees receive), and

    o Defined contribution plans (plans that define the employer contributions rather than the retirees' benefits).

  * The specific areas to be considered by the project include:

    o Determining an employer's pension obligation and the related cost,
    o Assigning that cost to specific accounting periods, and
    o Determining whether an employer participating in a multiemployer plan has a liability for unfunded defined benefits under the plan.

  * The FASB project will also consider accounting for other types of retirement benefits, such as continuation of life insurance and medical insurance after employees retire.

TECHNICAL AGENDA PROJECTS—For which Discussion Memoranda or Exposure Drafts have not been issued to date (Date placed on Agenda)

- Accounting by Employers for Pensions and Other Postemployment Benefits (March 1975)
  
  * Includes accounting for termination indemnities
— Financial Statements/Financial Reporting (1st Quarter 1978)
— Reporting Funds Flows and Liquidity (1st Quarter 1979)
  • Consideration of an enterprise’s funds flow and liquidity position and related information useful to financial statement users. Also reconsiders matters covered in APB Opinion No. 19, Reporting Changes in Financial Position.
— Reconsideration of the Conclusions of FASB Statement No. 8 (1st Quarter 1979)
— Accounting Recognition Criteria (2nd Quarter 1979)
  • Research reports are in progress
— Disclosure of Summarized Financial Information for All Material Investments Accounted for by the Equity Method (4th Quarter 1979)
— Determining Materiality for Capitalization of Interest Cost (January 30, 1980)
  • Would amend paragraph 8 of FASB Statement No. 34, Capitalization of Interest Cost to specify that a new test of materiality should not be applied in determining whether interest capitalization is required.

STAFF AGENDA PROJECTS—Not on FASB technical agenda at this date but under study by the Staff
— Lease Accounting Codification
— Current Text Codification

INTERPRETATIONS AND AMENDMENTS IN PROCESS—For which Discussion Memoranda or Exposure Drafts have not been issued
— FASB Statement No. 19 (Financial Accounting and Reporting by Oil and Gas Producing Companies)
  • Provision for deferred taxes on the difference between statutory depletion and book depletion

RESEARCH REPORTS IN PROCESS
— Timing of Recognition of Assets and Liabilities
  • Research is being conducted by Professor Yuji Ijiri of Carnegie-Mellon University.
— Recognition of Revenue and Expenses
  • Research is being conducted by Professor Henry Jaenicke of Franklin and Marshall College.
— Effects of FASB Statement No. 13, Accounting for Leases
  • Research is being conducted on the effect of Statement No. 13 on stock prices, bond risk premiums, and perceptions and actions of preparers and users of financial statements, and financial statement profiles. Research team is headed by A. Rashad Abdelkhalik of the University of Florida.
— Understanding How Investors, Creditors, and Other Users of Financial Information Make Decisions
  • Research is being conducted by the FASB staff.

OTHER MATTERS—Items proposed to the FASB by various parties but not yet placed on the FASB’s technical agenda

— Clarification of Reporting Practices Covering Hospital Related Organizations

— Accounting for Title Insurance Companies
  • The Board has expressed its intent to designate the specialized principles in the forthcoming AICPA Statement of Position, *Accounting for Title Insurance Companies*, as preferable for purposes of applying APB Opinion No. 20, *Accounting Changes*.

— Accounting for Repurchase Agreements
  • The Board decided that the AICPA should prepare a proposed Statement of Position concerning accounting for repurchase agreements entered into by financial institutions.

— FASB Statement No. 34, *Capitalization of Interest Cost*, and Potential Conflict with other Official Pronouncements
  • The FASB staff is investigating potential conflicts between Statement No. 34 and certain AICPA Accounting Guides, Audit Guides, and Statements of Position.

— New Basis ("Push Down") Accounting
  • A staff Technical Bulletin will be issued.