

1995

Securities industry developments - 1995/96; Audit risk alerts

American Institute of Certified Public Accountants. Auditing Standards Division

Follow this and additional works at: https://egrove.olemiss.edu/aicpa_indev

Part of the [Accounting Commons](#), and the [Taxation Commons](#)

Recommended Citation

American Institute of Certified Public Accountants. Auditing Standards Division, "Securities industry developments - 1995/96; Audit risk alerts" (1995). *Industry Developments and Alerts*. 191.
https://egrove.olemiss.edu/aicpa_indev/191

This Article is brought to you for free and open access by the American Institute of Certified Public Accountants (AICPA) Historical Collection at eGrove. It has been accepted for inclusion in Industry Developments and Alerts by an authorized administrator of eGrove. For more information, please contact egrove@olemiss.edu.



**AUDIT RISK
ALERTS**

Securities Industry Developments—1995/96

**Complement to AICPA Audit and Accounting Guide
*Audits of Brokers and Dealers in Securities***

AICPA

American Institute of Certified Public Accountants

NOTICE TO READERS

This Audit Risk Alert is intended to provide auditors of financial statements of brokers and dealers in securities with an overview of recent economic, industry, regulatory, and professional developments that may affect the audits they perform. This document has been prepared by the AICPA staff. It has not been approved, disapproved, or otherwise acted on by a senior technical committee of the AICPA.

Al Goll
Technical Manager, Accounting Standards Division

Gerard L. Yarnall
Director, Audit and Accounting Guides

The AICPA staff is grateful to the members of the AICPA Stockbrokerage and Investment Banking Committee for their contribution to this document.

Copyright © 1995 by
American Institute of Certified Public Accountants, Inc.,
New York, NY 10036-8775

All rights reserved. Requests for permission to make copies of any part of this work should be mailed to Permissions Department, AICPA, Harborside Financial Center, 201 Plaza Three, Jersey City, NJ 07311-3881.

1 2 3 4 5 6 7 8 9 0 AAG 998765

Table of Contents

	<u>Page</u>
Securities Industry Developments—1995/96	5
Industry and Economic Developments	5
Industry Trends	5
Regulatory and Legislative Developments	6
Changed Settlement Date	7
FOCUS Report Revision	8
Other SEC Concerns	8
CFTC Regulations	9
Audit Issues and Developments	10
Derivatives Activities	10
Valuation of Securities	11
Globalization	12
Service Auditors' Reports	13
Elimination of Uncertainty Reporting	14
Accounting Issues and Developments	14
Impairment of Long-Lived Assets	14
FASB Statement on Derivatives	16
FASB Interpretation—Offsetting	16
Audit and Accounting Guide	17
Information Sources	17

Securities Industry Developments—1995/96

Industry and Economic Developments

The securities industry appears to be on the upswing in 1995, after experiencing significant declines in 1994 revenues and earnings from the records set in 1993. Contributing to the upswing are—

- Increased fixed-income activity in the wake of a favorable interest-rate environment.
- Record levels of average daily volume on major exchanges.
- Strong underwriting activity as markets maintain record high levels.
- Continuing strength in merger and acquisition related work.

Securities analysts expect that brokerage firms will continue to generate strong profits for the balance of the year, especially if interest rates do not increase.

Industry Trends

The securities industry continues to be affected in a variety of ways by recent economic trends and developments. Some of the more pervasive trends that are likely to affect the operations of securities firms, and thereby influence audit risk, include the following.

Expansion of the Derivatives Products Market. The securities industry continues to play a major role in the market for derivative financial instruments—in terms of the types of products offered, the number of transactions, and the number of participants in the market. Many firms have established divisions or subsidiaries solely for the purpose of conducting business in derivatives. The innovative and complex nature of derivative products along with the rapid expansion of the market and limited authoritative accounting literature related to these entities and products may significantly increase audit risk.

Inadequate internal controls over transactions that involve complex financial instruments, coupled with highly sophisticated trading strategies, can significantly heighten audit risk. Recent instances of dis-

astrous consequences from this shortcoming are exemplified by the collapse of Barings PLC. In addition, broker-dealers who sell complex financial instruments may be subject to customers' claims for compensation for losses on such instruments, such as for the financial difficulties experienced by the government of Orange County, California. As they assess audit risk, auditors of financial statements of broker-dealers should consider the auditing ramifications of these and other developments significant to the industry. Regulators and major participants in the derivatives markets are taking the initiative to improve controls over these products. (See the "Regulatory and Legislative Developments", "Audit Issues and Developments", and "Accounting Issues and Developments" sections of this Audit Risk Alert, as well as *Audit Risk Alert—1995/96*, for further discussions of derivatives.)

Heightened Competition From Banks and Other Financial Services Entities. Banks, insurance companies, and other providers of financial services continue to present formidable competition to securities firms. Heightened competition is spurring consolidation activities in the industry. To maintain their home-field advantage and gain a foothold in lucrative emerging foreign markets, many firms are rounding out product lines through acquisitions.

Market Globalization. In the face of worldwide economic and ideological transformations and technological advances, as well as changes in the European Economic Community, the move toward globalization of the securities industry continues at break-neck speed. Many broker-dealers view gaining access to new markets as one of their top priorities for future growth. As a result, auditors may need to consider the ramifications of globalization on financial statements of broker-dealers. (See the "Audit Issues and Developments" section of this Audit Risk Alert.)

Regulatory and Legislative Developments

Regulation of broker-dealers is discussed in chapter 1 of the AICPA Audit and Accounting Guide *Audits of Brokers and Dealers in Securities*. The following discussion is intended to help auditors stay abreast of developments that affect the regulation of broker-dealers.

AICPA Statement on Auditing Standards (SAS) No. 22, *Planning and Supervision* (AICPA, *Professional Standards*, vol. 1, AU sec. 311), requires that, in planning their audits, auditors consider matters affecting the industry in which an entity operates, including, among other things, government regulations. Auditors consider such regulations in light of

their potential impact on the financial statements being audited. SAS No. 54, *Illegal Acts by Clients* (AICPA, *Professional Standards*, vol. 1, AU sec. 317), distinguishes between two types of laws and regulations:

1. Those that have a direct and material effect on the determination of financial statement amounts
2. Those that relate more to an entity's operating aspects than to its financial and accounting aspects and therefore have only an indirect effect on the financial statements

Although auditors should design their audits to provide reasonable assurance of detecting material misstatements of the financial statements resulting from illegal acts that directly and materially affect financial statement amounts, an audit performed in accordance with generally accepted auditing standards does not include procedures specifically designed to detect illegal acts that would have only indirectly affected financial statements. Nonetheless, auditors should be aware of the possibility that such illegal acts may have occurred.

The securities industry is subject to extensive regulations by a number of federal and state authorities. As a result, auditors of broker-dealers should be familiar with applicable rules and regulations of government agencies and other regulatory bodies, including the Securities and Exchange Commission (SEC) and industry member regulatory bodies (such as the National Association of Securities Dealers) and national securities exchanges (such as the New York Stock Exchange).

Auditors of broker-dealers that are also commodities brokers should consider rules and regulations of the Commodity Futures Trading Commission (CFTC). The CFTC was created by Congress in 1974 and is the federal agency with regulatory and oversight responsibility for the trading of commodity futures and options contracts on the U.S. futures exchanges. Since 1982, the CFTC has also regulated operations on futures contracts and options on physical commodities trading on commodity markets.

A summary of some of the recent regulatory developments that may affect the audits of broker-dealers follows.

Changed Settlement Date

On June 7, 1995, Rule 15c6-1 of the Securities and Exchange Act of 1934, establishing three business days after the trade date (T+3) instead of five business days as the standard settlement time frame for most broker-dealer transactions, became effective. The rule covers transactions in all securities other than exempted securities, government securities, municipal securities, commercial paper, bankers' acceptances, or commercial bills. The rule contains a specific exemption for sales of

unlisted limited-partnership interests and contains alternative settlement time frames for certain firm commitment offerings of new issues.

FOCUS Report Revision

The Financial and Operational Combined Uniform Single (FOCUS) report is the uniform regulatory report required to be filed with regulators by broker-dealers. Some parts of the report are to be filed monthly, some quarterly, and some annually. Audited financial statements must be filed with the report annually. The staffs of the SEC and the CFTC, in cooperation with the Capital Committee of the Securities Industry Association, are revising the report. The CFTC permits futures commission merchants (FCMs) who are also registered broker-dealers to file the FOCUS report instead of the currently required CFTC Form 1-FR. After the revised FOCUS report has been approved for use, the CFTC intends to allow FCMs, whether or not they are broker-dealers, to file CFTC reports using the new FOCUS report. The revised report is expected to prohibit broker-dealers from including subordinated debt in a combined total with equity on the balance sheet. However, no change is anticipated that would prohibit including qualifying subordinated debt in regulatory net capital. Auditors should be alert to the issuance of final regulations specifying the revised reporting requirements.

Other SEC Concerns

The SEC's Division of Market Regulation has noted, in various public forums, the matters in the following sections that frequently incur comments on materials filed with the SEC or that have been identified by the SEC's field inspection process. If auditors become aware during the course of audits that such transactions have not been reported in the financial statements as recommended, they should consider the effect on the amounts presented in the financial statements of such deviations and whether, in accordance with SAS No. 54, the audit committee or others with equivalent authority or responsibility are adequately informed about the matter.

Derivatives and Other High-Risk Investments. The joint Statement of the SEC, the CFTC and the Securities and Investments Board emphasized the importance of management controls over derivatives and the need for improved accounting and disclosure rules for derivatives. It listed the following concepts that management controls should include:

-
1. Policies about derivative activities should be promulgated by the board of directors and should be reviewed as business and market circumstances change.
 2. Execution of these policies should be supported by valuation procedures and techniques, risk management and information systems designed to ensure the adequacy of both management information and external reporting.
 3. Responsibility for implementing the policies should be clearly delineated and the board of directors should define appropriate levels of and delegated authority for those responsible for implementing board policies for supervising over-the-counter (OTC) derivatives activities.
 4. Information systems should be designed to achieve full compliance with the policies and principles, assist in the active management of derivatives activities, and provide an adequate flow of relevant information about the derivatives activities not only of the firm but also of its related entities on a worldwide basis.
 5. Appropriate expertise should be maintained at all levels of a firm.
 6. Internal controls should include units, which are independent of trading personnel and report directly to senior management, dedicated to the evaluation of credit, market, and legal risks.
 7. Appropriate use should be made of risk-reduction techniques, such as master agreements and credit enhancements, including collateralization.

CFTC Regulations

Risk Assessment Rules. The CFTC has approved Regulations 1.14 and 1.15, which entail, respectively, certain recordkeeping and reporting requirements for FCMs that are part of a holding-company system. The requirements relate to risk assessment information covering the financial activities of the FCM's affiliates. The rules are designed to enhance the CFTC's financial surveillance program by providing the CFTC with increased access to material information concerning the activities of the affiliates of an FCM that may expose the FCM to financial or operational risks. The rules were effective on December 31, 1994, with initial filings for firms with a December 31 year-end due May 15, 1995.

Revised Disclosure Framework. The CFTC has adopted substantial revisions to the disclosure framework applicable to commodity pool operators (CPOs) and commodity trading advisors (CTAs). The revisions

are intended to achieve greater simplicity, focus, and clarity in performance history; streamline other required disclosures; improve the presentation and understandability of disclosures to investors; and create a more concise and readable format for disclosure documents. The rules are effective for filings made after August 24, 1995. CPOs and CTAs sometimes request that auditors report on their performance statistics. Auditors performing such engagements should follow the guidance in the AICPA Notice to Practitioners *Examination Engagements to Report on Investment Performance Statistics Based on Established or Stated Criteria*. The Notice amends the guidance provided in a previously issued Notice to Practitioners, *Engagements to Report on Performance Presentation Standards of the Association for Investment Management and Research*. It provides practical applications of the reporting example included in paragraph 54 of AICPA Statement on Standards for Attestation Engagements No. 1, *Attestation Standards* (AICPA, *Professional Standards*, vol. 1, AT sec. 100). (To obtain this Notice to Practitioners, dial (201) 938-3787 from a fax machine, follow the voice cues, and select document number 477.)

Audit Issues and Developments

Derivatives Activities

Recent years have seen a growing use of the innovative financial instruments commonly referred to as derivatives. They are often very complex and can involve a substantial risk of loss. Broker-dealers both create and sell derivative financial products and use such instruments as risk management tools (hedged) or as speculative investment vehicles. As interest rates, commodity prices, and numerous other market rates and indices from which derivative financial instruments obtain their value have increased in volatility, a number of entities have incurred significant losses as a result of their use. The use of derivatives almost always increases audit risk. Although the financial statement assertions about derivatives are generally similar to assertions about other transactions, the auditors' approach to achieving related audit objectives may differ because certain derivatives are not generally recognized in the financial statements.

Broker-dealers that sell derivative financial instruments are increasingly at risk for their sales practices and the acceptability of the methodology used to value derivatives at any point in time when requested to do so by their customers. In several cases, customers who have suffered large derivative-related losses have sued, alleging fraud and deception in sales practices or valuation. Determining the fair value of a

derivative financial instrument related to a customized transaction can involve complex calculations. These calculations often require various quantitative assumptions and complex modeling, and are further complicated by subjective value adjustments, such as the credit risk associated with the specified counterparty.

It is essential that auditors understand both the economics of derivatives used by the entities whose financial statements they audit and the nature and business purpose of the entities' derivatives activities. In addition, auditors should evaluate their client's accounting for any such instruments, especially those carried at other than market value. To the extent the derivatives qualify as financial instruments as defined in Financial Accounting Standards Board (FASB) Statement No. 105, *Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk* (FASB, *Current Text*, vol. 1, sec. F25), FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments* (FASB, *Current Text*, vol. 1, sec. F25), and FASB Statement No. 119, *Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments* (FASB, *Current Text*, vol. 1, sec. F25), the disclosure requirements set forth in those Statements must be met. When derivatives are accounted for as hedges of on-balance-sheet assets or liabilities or of anticipated transactions, auditors should review the appropriateness of the use of hedge accounting, particularly considering whether the criteria set forth in appropriate accounting literature are present.

The SEC staff has indicated that publicly held companies should disclose the nature and purpose of certain commodity-based derivatives activities, the nature and terms of certain commodity-based derivatives used, and the accounting methods used even when such derivatives do not meet the definition of financial instruments set forth in the FASB Statements cited above.

Many of the unique audit risk considerations presented by the use of derivatives are discussed in detail in *Audit Risk Alert—1995/96*. Also, see "FASB Statement on Derivatives" in the "Accounting Issues and Developments" section of this Audit Risk Alert. The AICPA publication *Derivatives-Current Accounting and Auditing Literature* (Product No. 014888) summarizes current authoritative accounting and auditing guidance and provides background information on basic derivatives contracts, risks, and other general considerations.

Valuation of Securities

The valuation of investment securities continues to be a prime concern for auditors of broker-dealers. Investments generally represent the most significant asset in a broker-dealer's statement of condition.

Chapter 4 of *Audits of Brokers and Dealers in Securities* describes the estimation of fair values of securities in good faith by management. In auditing securities' valuations determined by management, auditors should review the information considered by management in determining the value of the securities, ascertain that the procedures followed were reasonable, and read relevant minutes. In some instances, auditors may consider using the work of a specialist in auditing the valuation of such securities. SAS No. 73, *Using the Work of a Specialist* (AICPA, *Professional Standards*, vol. 1, AU sec. 336), provides guidance for when auditors decide to consider the work of any specialist used. Auditing the valuation of such securities is an area that requires a high degree of judgment and scrutiny to ensure that the carrying amounts approximate fair value.

Globalization

With the continuing trend to globalization of securities markets, auditors should be alert to factors that affect financial statements of broker-dealers effecting transactions in foreign securities. The following effects on broker-dealers' financial statements should be considered:

- There are custody issues related to the receipt and delivery of securities, the collections and payments of dividends and interest, information gathering, and processing with regard to corporate actions. Foreign custody agents must qualify under SEC Rule 17f-4, which governs the eligibility of depositories.
- Custody requirements vary by country. Settlement cycles, as well as holiday schedules, are usually different. Seldom, other than in the United States, does the exchange of shares for money take place simultaneously. In some clearing environments, the actual delivery of shares takes place more than twenty-four hours before payment. Therefore, counterparty risk and the process for choosing counterparties are important factors.
- The means of settling transactions in different countries can be dissimilar. Depending on the marketplace, book shares, physical shares (both registered and bearer), issuers' receipts, or transfer agent receipts may be the norm for transfer of ownership.
- Trading in offshore markets may involve the use of corresponding foreign exchange (FX) transactions to convert into the local currency of the foreign market. Such an FX transaction is another contract with its own risks and liabilities.

-
- Each country has its own unique rules relating to certain exception-type transactions. The issues here may be whether short sales are allowed in the trading environment, if a stock loan is a business in that market, and what the regulatory issues relating to contract closeouts are.
 - Tax and regulatory issues within a foreign market are another of the considerations to review. Issues relating to withholding of taxes, principal and income repatriation, and proper registrations are important within that market. The U.S. rules as they relate to a U.S. broker-dealer transacting business in the international marketplace are also a variable that affects business.

Service Auditors' Reports

Broker-dealers frequently use the services of fund custodians, transfer agents, and other service organizations that affect assertions in a broker-dealer's financial statements. In obtaining an understanding of a broker-dealer's internal control structure and assessing control risk, auditors should consider the functions or processing performed by such service organizations. SAS No. 70, *Reports on the Processing of Transactions by Service Organizations* (AICPA, *Professional Standards*, vol. 1, AU sec. 324), provides guidance to auditors of entities that use service organizations and may be applicable to audits of broker-dealers.

SAS No. 55, *Consideration of the Internal Control Structure in a Financial Statement Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 319), requires an auditor to obtain a sufficient understanding of an entity's internal control structure to plan the audit. When a broker-dealer uses a service organization, control structure policies and procedures at the service organization that affect the functions or processing performed by the service organization may have a significant effect on assertions in the broker-dealer's financial statements. For this reason, planning the audit of a broker-dealer may require that the auditor gain an understanding of the control structure policies and procedures performed by a service organization. When a broker-dealer relies on a service organization's control structure policies and procedures over the processing of transactions that are material to the broker-dealer's financial statements, these policies and procedures should be considered by the auditor. One method of obtaining information about these policies and procedures is to obtain a service auditor's report as described in SAS No. 70.

The AICPA's Auditing Standards Division will issue an Auditing Procedure Study titled *Implementing SAS No. 70, Reports on the Processing of Transactions by Service Organizations*, by the end of 1995.

Elimination of Uncertainty Reporting

The AICPA's Auditing Standards Board (ASB) has issued an exposure draft of a proposed SAS, *Amendment to Statement on Auditing Standards No. 58, Reports on Audited Financial Statements*, that would eliminate the requirement that, when certain criteria are met, the auditor add an uncertainties explanatory paragraph to the auditor's report.

The amendment would also expand the guidance in paragraph 37 of SAS No. 58, *Reports on Audited Financial Statements* (AICPA, *Professional Standards*, vol. 1, AU sec. 508), to indicate that "unusually important risks or uncertainties associated with contingencies, significant estimates, or concentrations" are matters that auditors may wish to emphasize in their reports. The amendment retains the option allowing auditors to disclaim an opinion on financial statements due to uncertainties.

The proposal does not affect the provisions of SAS No. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (AICPA, *Professional Standards*, vol. 1, AU sec. 341), which requires that the auditor add an explanatory paragraph to the auditor's report when there is substantial doubt about the entity's ability to continue as a going concern.

Audits of Brokers and Dealers in Securities indicates that auditors of the financial statements of broker-dealers may consider it necessary to add an uncertainty explanatory paragraph to their reports when the financial statements contain securities whose values were estimated by the board of directors in the absence of readily ascertainable market values and the range of possible values of those securities is significant. If the proposed SAS is issued in final form, that requirement will be eliminated. Nonetheless, auditors reporting on financial statements that include such securities may wish to emphasize that fact by adding an emphasis-of-a-matter paragraph to their reports. Such paragraphs, however, are optional and are added solely at the auditor's discretion.

The ASB hopes to finalize this SAS late this year and to issue an SAS that would be effective for reports issued on or after June 30, 1996. Comments on the proposed SAS were due on October 20, 1995.

Accounting Issues and Developments

Impairment of Long-Lived Assets

In March 1995, the FASB issued Statement No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of* (FASB, *Current Text*, vol. 1, sec. 108). FASB Statement No. 121 establishes accounting standards for the impairment of long-lived assets,

certain identifiable intangibles, and goodwill related to those assets to be held and used and for long-lived assets and certain identifiable intangibles to be disposed of. The Statement requires that long-lived assets and certain identifiable intangibles to be held and used by an entity be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In performing the review for recoverability, the Statement requires that the entity estimate the future cash flows expected to result from the use of the asset and its eventual disposition. If the sum of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the asset, an impairment loss is recognized. Otherwise, an impairment loss is not recognized. Measurement of an impairment loss for long-lived assets and identifiable intangibles that an entity expects to hold and use should be based on the fair value of the asset. (The fair value of an asset is the amount at which that asset could be bought or sold in a current transaction between willing parties.)

The Statement also requires that long-lived assets and certain identifiable intangibles to be disposed of be reported at the lower of carrying amount or fair value less cost to sell, except for assets covered by Accounting Principles Board (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* (FASB, *Current Text*, vol. 1, sec. I13). Assets covered by APB Opinion No. 30 will continue to be reported at the lower of the carrying amount or the net realizable value.

The Statement is effective for financial statements for fiscal years beginning after December 15, 1995. Restatement of previously issued financial statements is not permitted by the Statement. The Statement requires that impairment losses resulting from its application be reported in the period in which the recognition criteria are first applied and met. The Statement requires that initial application of its provisions to assets that are being held for disposal at the date of adoption should be reported as the cumulative effect of a change in accounting principle.

Auditors of broker-dealers should be aware that the current industry climate of restructurings, mergers, and realignments have increased the likelihood that events or changes in circumstances that indicate that assets have been impaired may have occurred. For example, a merger may result in the reduction of services provided by a particular entity within the combined organization and significantly reduce its ability to generate future cash flows. In this instance, the carrying amounts of recorded assets may not be recoverable and the provisions of FASB Statement No. 121 may need to be applied.

In considering a broker-dealer's implementation of FASB Statement No. 121, auditors should obtain an understanding of the policies and procedures used by management to determine whether all impaired assets have been properly identified. Management's estimates of future cash flows from asset use and impairment losses should be evaluated pursuant to the guidelines set forth in SAS No. 57, *Auditing Accounting Estimates* (AICPA, *Professional Standards*, vol. 1, AU sec. 342).

FASB Statement on Derivatives

In October 1994, the FASB issued Statement No. 119. FASB Statement No. 119 requires disclosures about derivative financial instruments—futures, forward, swap, and option contracts, and other financial instruments with similar characteristics. It also amends existing requirements of FASB Statements No. 105 and No. 107.

The Statement requires disclosures about amounts, nature, and terms of derivative financial instruments that are not subject to FASB Statement No. 105 because they do not result in off-balance-sheet risk of accounting loss. It requires that a distinction be made between financial instruments held or issued for trading purposes (including dealing and other trading activities measured at fair value, with gains and losses recognized in earnings) and financial instruments held or issued for purposes other than trading. Paragraph 12 of FASB Statement No. 119 encourages, but does not require, entities to disclose quantitative information about risks associated with derivatives.

FASB Statement No. 119 was effective for financial statements issued for fiscal years ending after December 15, 1994, except for organizations with less than \$150 million in total assets. For those organizations, the Statement is effective for financial statements issued for fiscal years ending after December 15, 1995.

The FASB Special Report, *Illustrations of Financial Instrument Disclosures*, contains illustrations of the application of FASB Statements No. 105, No. 107, and No. 119.

FASB Interpretation—Offsetting

The FASB issued Interpretation No. 41, *Offsetting of Amounts Related to Certain Repurchase and Reverse Repurchase Agreements* (FASB, *Current Text*, vol. 1, sec B10), in December 1994. APB Opinion No. 10, *Omnibus Opinion—1966*, paragraph 7 (FASB, *Current Text*, vol. 1, sec. B10), states that "it is a general principle of accounting that the offsetting of assets and liabilities in the balance sheet is improper except where a right of setoff exists." FASB Interpretation No. 39, *Offsetting of Amounts Related*

to *Certain Contracts* (FASB, *Current Text*, vol. 1, sec. B10), defines *right of setoff* and specifies conditions that must be met to permit offsetting. This Interpretation modifies Interpretation No. 39 to permit offsetting in the statement of financial position of payables and receivables that represent repurchase agreements and reverse repurchase agreements and that meet the conditions of the Interpretation.

This Interpretation is effective for financial statements issued for periods ending after December 15, 1994.

Audit and Accounting Guide

In 1996, the AICPA expects to issue an *Audit and Accounting Guide Brokers and Dealers in Securities*, which will supersede the current *Audit and Accounting Guide Audits of Brokers and Dealers in Securities*. The new Guide will discuss those aspects of accounting and auditing unique to brokers and dealers in securities. It also incorporates new accounting and financial reporting requirements issued by the FASB and the AICPA's Accounting Standards Executive Committee, as well as new auditing standards issued by the ASB since issuance of the superseded guide.

The new Guide is expected to provide for two changes in financial reporting: (1) it will no longer permit combining of subordinated debt with stockholders' equity and (2) it will require that delayed delivery transactions be reported in the statement of condition on the settlement (delivery) date instead of on the trade date. The changes are tentatively effective for annual financial statements issued for fiscal years ending after June 15, 1996.

Information Sources

Further information on matters addressed in this risk alert is available through various publications and services listed in the table at the end of this document. Many non-government and some government publications and services involve a charge or membership requirement.

Fax services allow users to follow voice cues and request that selected documents be sent by fax machine. Some fax services require the user to call from the handset of the fax machine, others allow users to call from any phone. Most fax services offer an index document, which lists titles and other information describing available documents.

Electronic bulletin board services allow users to read, copy, and exchange information electronically. Most are available using a modem and standard communications software. Some bulletin board services are also available using one or more Internet protocols.

Recorded announcements allow users to listen to announcements about a variety of recent or scheduled actions or meetings.

All phone numbers listed are voice lines, unless otherwise designated as fax (f) or data (d) lines. Required modem speeds, expressed in bauds per second (bps), are listed data lines.

* * * *

This Audit Risk Alert supersedes *Securities Industry Developments—1994*.

* * * *

Practitioners should also be aware of the economic, industry, regulatory, and professional developments as described in *Audit Risk Alert—1995/96* and *Compilation and Review Alert—1995/96*, which may be obtained by calling the AICPA Order Department and asking for product number 022180 (audit) or 060669 (compilation and review).

Information Sources

Organization	General Information	Fax Services	Electronic Bulletin Board Services	Recorded Announcements
American Institute of Certified Public Accountants	<p><i>Order Department</i> Harborside Financial Center 201 Plaza Three Jersey City, NJ 07311-3881 (800) TO-AICPA or (800) 862-4272</p> <p>Information about AICPA continuing professional education programs is available through the AICPA CPE Division (ext. 3) and the AICPA Meetings and Travel Division: (201) 938-3232.</p>	<p><i>24 Hour Fax Hotline</i> (201) 938-3787</p>	<p><i>Accountants Forum</i> This information service is available on CompuServe. Some information is available only to AICPA members. To set up a CompuServe account call (800) 524-3388 and ask for the AICPA package or rep. 748.</p>	
Financial Accounting Standards Board	<p><i>Order Department</i> P.O. Box 5116 Norwalk, CT 06856-5116 (203) 947-0700, ext. 10</p>			Action Alert Telephone Line (203) 847-0700 (ext. 444)
U.S. Securities and Exchange Commission	<p><i>Publications Unit</i> 450 Fifth Street, NW Washington, DC 20549-0001 (202) 942-4046 <i>SEC Public Reference Room</i> (202) 942-8079</p>	<p><i>Information Line</i> (202) 942-8088 (ext. 3) (202) 942-7114 (tty)</p>		Information Line (202) 942-8088 (202) 942-7114 (tty)
Commodity Futures Trading Commission	<p>Three Lafayette Center 1155 21st Street, NW Washington, DC 20581 (202) 418-5459 (Office of Chief Accountant Div. of Trading & Markets)</p>	(202) 418-5528		

(continued)

Information Sources (cont'd)

Organization	General Information	Fax Services	Electronic Bulletin Board Services	Recorded Announcements
Securities Industry Association	120 Broadway New York, NY 10271-0080 (212) 608-1500	(212) 608-1604		
New York Stock Exchange, Inc.	Eleven Wall Street New York, NY 10005 (212) 656-3000	(212) 656-2126		
National Association of Securities Dealers, Inc.	1735 K Street, NW Washington, DC 20006-1500 (202) 728-8000			

