

University of Mississippi

eGrove

---

Newsletters

American Institute of Certified Public  
Accountants (AICPA) Historical Collection

---

1-1999

## AcSec Update, Volume 3, Number 1 January 1999

American Institute of Certified Public Accountants. Accounting Standards Executive Committee

Follow this and additional works at: [https://egrove.olemiss.edu/aicpa\\_news](https://egrove.olemiss.edu/aicpa_news)



Part of the [Accounting Commons](#)

---

# AcSEC UPDATE

A publication of the Accounting Standards Executive Committee of the AICPA

AICPA

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

## AcSEC ISSUES TWO NEW SOPs

### Deposit Accounting

In December 1998, AcSEC issued SOP 98-7, *Deposit Accounting: Accounting for Insurance and Reinsurance Contracts That Do Not Transfer Insurance Risk* (product no. 014909). This SOP provides guidance on how to account for insurance and reinsurance contracts that do not transfer insurance risk. It applies to all entities and all insurance and reinsurance contracts that do not transfer insurance risk, except for long-duration life and health insurance contracts. The method used to account for insurance and reinsurance contracts that do not transfer insurance risk is referred to in the SOP as deposit accounting. SOP 98-7 does not address when deposit accounting should be applied.

This SOP is effective for fiscal years beginning after June 15, 1999, with earlier application encouraged.

### Software Revenue Recognition

In December 1998, AcSEC issued SOP 98-9, *Modification of SOP 97-2, "Software Revenue Recognition," With Respect to Certain Transactions* (product no. 014920). This SOP amends paragraphs 11 and 12 of SOP 97-2, *Software Revenue Recognition*, to require recognition of revenue using the "residual method" when (1) there is vendor-specific objective evidence of the fair values of all undelivered elements in a multiple-element arrange-

ment that is not accounted for using long-term contract accounting, (2) vendor-specific objective evidence of fair value does not exist for one or more of the delivered elements in the arrangement, and (3) all revenue-recognition criteria in SOP 97-2 other than the requirement for vendor-specific objective evidence of the fair value of each delivered element of the arrangement are satisfied. Under the residual method, the arrangement fee is recognized as follows: (1) the total fair value of the undelivered elements, as indicated by vendor-specific objective evidence, is deferred and subsequently recognized in accordance with the relevant sections of SOP 97-2 and (2) the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements.

Effective December 15, 1998, this SOP amends SOP 98-4, *Deferral of the Effective Date of a Provision of SOP 97-2, "Software Revenue Recognition,"* to extend the deferral of the application of certain passages of SOP 97-2 provided by SOP 98-4 through fiscal years beginning on or before March 15, 1999.

All other provisions of SOP 98-9 are effective for transactions entered into in fiscal years beginning after March 15, 1999. Earlier adoption is permitted as of the beginning of fiscal years or interim periods for which financial statements or information have not been issued; retroactive application is prohibited. ♦

## RECENT MEMBER ACTIVITIES

### *Speeches by AcSEC Members*

**Robert Dale** — “AcSEC Activities Update,” University of Florida Accounting Conference, Gainesville, FL, November 1998.

**David Kaplan** — “Panel Presentation – Midwest Financial Symposium,” Illinois CPA Society, Chicago, IL, October 1998;

“The Role of AcSEC in the Accounting Standard Setting Process,” Financial Accounting Standards Advisory Council, Norwalk, CT, October 1998;

“AcSEC Update,” Ninth Annual Conference on Financial Reporting, University of California at Berkeley, San Francisco, CA, October 1998;

“AcSEC Update,” AICPA National Conference on Banks and Savings Institutions, Washington, DC, November 1998;

“AcSEC Update,” Financial Reporting Issues Conference, Financial Executives Institute, New York, NY, November 1998;

“Accounting for Enterprise Systems Projects,” Financial Reporting Issues Conference, Financial Executives Institute, New York, NY, November 1998;

“AcSEC Update,” AICPA National Conference on Current SEC Developments, Washington, DC, December 1998.

**Louis Matusiak, Jr.** — “AcSEC Activities Update,” Auditing and Accounting Symposium of The American Group, Scottsdale, AZ, November 1998.

**David Morris** — “Derivatives Reporting to Senior Management,” Executives Enterprises, New York, NY, October 1998.

**Paula Panik** — “National Association of Insurance Commissioners (NAIC): An Update on Codification,” Insurance Industry Conference of the Connecticut Society of CPA's, Hartford, CT, November 1998. ♦

## RECENT AcSEC ACTIVITIES

**Life and Health Insurance Entities** On September 4, 1998, the AICPA released for public comment a proposed Audit and Accounting Guide, *Life and Health Insurance Entities*. The proposed Guide would supersede the AICPA Industry Audit Guide, *Audits of Stock Life Insurance Companies*, issued in 1972 as updated only for conforming changes. The comment deadline was December 4, 1998. AcSEC is scheduled to discuss the comment letters at its April 1999 meeting.

The proposed Guide discusses those aspects of accounting and auditing unique to life and health insurance entities and was developed to assist life and health insurance entities in preparing financial statements in conformity with GAAP and to assist independent auditors in auditing and reporting on those financial statements. In addition, the proposed Guide contains significant discussions of statutory accounting practices (SAP) that include laws, regulations, and administrative rulings adopted by various states that govern the operations and reporting requirements of life insurance entities. The proposed Guide does not reflect SAP under the National Association of Insurance Commissioners codification project. The relevant SAP section in the proposed Guide is currently being updated to reflect those standards.

The proposed Guide also incorporates accounting and financial reporting requirements issued by the FASB and AcSEC since the issuance of the AICPA Industry Audit Guide *Audits of Stock Life Insurance Companies*. Also incorporated in this proposed Guide are new auditing standards issued by the AICPA Auditing Standards Board since the issuance of the pronouncements that the proposed Guide would supersede.

The Life and Health Insurance Entities Audit and Accounting Guide is not intended to establish any new accounting standards or interpret any existing accounting standards, except for the inclusion of an SEC staff announcement regarding the effects of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, made at the July 12, 1994 EITF meeting, on certain assets and liabilities.

**Investment Companies** On September 22, 1998, AcSEC issued an exposure draft of a completely revised Audit and Accounting Guide, *Audits of Investment Companies*. This proposed Guide will replace the AICPA Audit and Accounting Guide, *Audits of*

*Continued on page 3*

**Editor: Marc Simon**

**Administrative Editor: Sharon Macey**

AcSEC Update, the newsletter of the AICPA Accounting Standards Executive Committee, is published three times a year.

Copyright © 1998 American Institute of Certified Public Accountants, Inc. The views expressed herein are those of the authors and do not necessarily reflect the views of the American Institute of Certified Public Accountants. Official positions of the AICPA are determined through specific committee procedures, due process, and deliberation.



## RECENT AcSEC ACTIVITIES continued

*Investment Companies*, issued in 1987 as updated only for conforming changes. The proposed Guide is intended to address how to enhance the usefulness of investment company financial statements for their users. Among other things, it will provide new guidance on accounting for offering costs, amortization of premium or discount on bonds, liabilities for excess expense plans, and reporting complex capital structures. The comment deadline was December 22, 1998. AcSEC is scheduled to discuss the comment letters at its April 1999 meeting.

Most of the changes in accounting and financial reporting proposed by this Guide should be applied prospectively and are effective for annual financial statements issued for fiscal years beginning after December 15, 1999, and for interim financial statements issued after initial application. Earlier application is permitted. Restatement of previously issued financial statements is not permitted.

**Discounts Related to Credit Quality** On December 30, 1998, AcSEC issued an exposure draft for a proposed SOP, *Accounting for Discounts Related to Credit Quality*. Comments are due by April 29, 1999. See page 5 for details on the project.

**Motion Pictures** On October 16, 1998, AcSEC issued an exposure draft for a proposed SOP, *Accounting by Producers and Distributors of Films*. Comments were due by January 18, 1999. See page 7 for details on the project.

**401(h) Features** On September 9, 1998, AcSEC issued an exposure draft for a proposed SOP, *Accounting and Reporting of 401(h) Features of Defined Benefit Pension Plans*. Comments were due by December 9, 1998. See pages 5-6 for details on the project. ❖

## To Order Copies of AcSEC Pronouncements

**Write:** AICPA Order Department, NQ, P.O. Box 2209, Jersey City, NJ 07303-2209; **order via fax,** 800-362-5066; or **call** 888-777-7077 (option #1). Ask for Operator NQ. Orders for exposure drafts must be written or faxed.

## EFFECTIVE DATES

SOP 97-3, *Accounting by Insurance and Other Enterprises for Insurance-Related Assessments*, for fiscal years beginning after December 15, 1998, with early adoption encouraged.

SOP 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, for years beginning after December 15, 1998, with earlier application encouraged in fiscal years for which annual financial statements have not been issued.

SOP 98-2, *Accounting for Costs of Activities of Not-for-Profit Organizations and State and Local Governmental Entities That Include Fund Raising*, for years beginning on or after December 15, 1998, with earlier application encouraged in fiscal years for which financial statements have not been issued.

SOP 98-4, *Deferral of the Effective Date of a Provision of SOP 97-2, "Software Revenue Recognition,"* as of March 31, 1998.

SOP 98-5, *Reporting on the Costs of Start-Up Activities*, for years beginning after December 15, 1998, with earlier application encouraged in fiscal years for which annual financial statements have not been issued.

SOP 98-7, *Deposit Accounting: Accounting for Insurance and Reinsurance Contracts That Do Not Transfer Insurance Risk*, for fiscal years beginning after June 15, 1999, with earlier adoption encouraged.

SOP 98-9, *Modification of SOP 97-2, "Software Revenue Recognition," With Respect to Certain Transactions*, extends the deferral of the application of certain passages of SOP 97-2 provided by SOP 98-4, *Deferral of the Effective Date of a Provision of SOP 97-2, "Software Revenue Recognition,"* effective December 15, 1998 to March 15, 1999; all other provisions are effective for transactions entered into in fiscal years beginning after March 15, 1999. Earlier adoption is permitted as of the beginning of fiscal years or interim periods for which financial statements or information have not been issued.

## AcSEC AGENDA PROJECTS

As of December 31, 1998	1998	1999		
	4Q	1Q	2Q	3Q
<b>General Applicability</b>				
Certain Managed Care — SOP (page 5)				
Deposit Accounting for Certain Reinsurance Contracts — SOP (page 1)	F			
<b>Computer Software</b>				
SOP 97-2 Amendment — SOP (page 1)	F			
<b>Lending Institutions</b>				
Discounts Related to Credit Quality — SOP (page 5)	E			
Banks and Savings Institutions, Credit Unions, and Finance Companies — SOP (page 6)		E		
<b>Employee Benefits Plans</b>				
Cost Sharing and Benefit Reduction Arrangements — SOP (page 5)			E	
401(h) Features — SOP (page 5)			F	
Investments and Other Disclosure Matters — SOP (page 5)		E		
<b>Investment Industry</b>				
Investment Companies — Guide (page 2)				F
<b>Insurance Industry</b>				
Life and Health Insurance Entities — Guide (page 2)				F
Mass Tort Exposures — SOP (page 6)				E
Nontraditional Contracts — SOP (page 8)				E
<b>Motion Picture Industry</b>				
Motion Pictures — SOP (page 7)	E			
<b>Real Estate Industry</b>				
Real Estate Investments — SOP (page 8)				
Real Estate Timesharing Arrangements — SOP (page 8)			E	
Real Estate Cost Capitalization — SOP (page 8)				

Codes: E—Exposure Draft Issued  
F—Final Pronouncement Issued

## AcSEC's CURRENT SOP PROJECTS

### Accounting for Discounts Related to Credit Quality

**Description and background.** FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*, requires that discounts be recognized as an adjustment of yield over an instrument's life. Practice Bulletin (PB) 6 further addresses accretion of discounts on certain acquired loans, which involves intertwining issues of accretion of discount, measurement of credit losses, and recognition of interest income. This project considers whether PB 6's objectives and guidance continue to be relevant given a number of FASB pronouncements issued subsequent to PB 6 to address various related issues.

The project addresses, for loans and debt securities purchased at a discount related to credit quality, the following issues:

- Investors would be prohibited from displaying discounts on purchased loans in the balance sheet. In other words, investors would not carry over the allowance for loan losses established by the seller.
- The investor would estimate expected cash flows on the loan at inception and periodically over the life of the loan. The excess of expected cash flows over the initial investment (purchase price) would be recognized as the loan's yield. The excess of contractual cash flows over expected cash flows would not be recognized as an adjustment of yield. Subsequent decreases in expected cash flows would result in recognition of an impairment. Subsequent increases in expected cash flows would be recognized prospectively.
- Loans purchased at a discount related to credit quality would not be considered impaired at acquisition for either measurement or disclosure purposes. However, the proposed SOP requires new disclosures for purchased loans within its scope, in addition to those already required by other accounting literature, including FASB Statement Nos. 114 and 118. Such disclosures apply whether or not loans are considered impaired.
- The proposed SOP would explicitly exclude originated loans from its scope. FASB Statement No. 125 provides criteria for distinguishing between purchased and originated loans. The proposed SOP also excludes transactions in which the investor acquires loans from the transferor through an agency relationship, for example, when the transferor bears no risk of loss in making and selling the loans.

**Current developments and plans.** In October 1998, FASB did not object to AcSEC issuing the proposed SOP for exposure. The exposure draft was issued December 30, 1998 and comments are due by April 29, 1999.

Staff: Brad Davidson

### Certain Managed Care Arrangements

**Description and background.** This project was undertaken in response to recent structural and operational changes occurring throughout the health care and insurance industries. The proposed SOP would address whether substantive differences in accounting for similar transactions entered into by health care organizations and insurance organizations should continue. The proposed SOP would amend the audit and accounting guide *Health Care Organizations* and SOP 89-5, *Financial Accounting and Reporting of Prepaid Healthcare Services*, and it could amend *Audits of Stock Life Insurance Companies*. The SOP would apply to all nongovernmental entities and potentially to certain governmental entities.

The project addresses the following issues:

- *Bifurcation.* Should revenues be bifurcated between premiums and administrative fees?
- *Reinsurance.* Should reinsurance transactions be presented gross or net in the income statement?
- *Accounting for loss contracts.* For purposes of determining whether a premium deficiency exists: How should contracts be grouped? How should costs that do not vary with a contract or group of contracts be treated? Should anticipated investment income be considered?
- *Incurred-but-not-reported (IBNR) Claims.* Which costs should be accrued as incurred-but-not-reported (IBNR) claims?
- *Deferred acquisition costs.* Should acquisition costs be capitalized? If so, which costs should be eligible for capitalization?

**Current developments and plans.** At its July 1998 meeting, AcSEC discussed concerns at the FASB regarding tentative conclusions reached by AcSEC related to the recognition of liabilities for IBNR claims—accruing costs of services provided during the period. AcSEC members agreed that the task force should pursue an approach that would recognize liabilities for the costs associated (for the contract period) with known conditions, provided that an appropriate revenue and profit recognition model also is developed. An exposure draft is expected in the fourth quarter of 1999.

Staff: Joel Tanenbaum

### Employee Benefit Plans

This project, which now consists of three proposed SOPs, would amend the Audit and Accounting Guide *Audits of Employee Benefit Plans*, SOP 92-6, *Accounting and Reporting by Health and Welfare Benefit Plans*, and SOP 94-4, *Reporting of Investment Contracts Held by Health and Welfare Benefit Plans and Defined Contribution Plans*, and would supersede PB 12, *Reporting Separate Investment Fund Option Information of Defined-Contribution Pension Plans*.

Continued on page 6



**Description and background.** The first SOP, *Accounting and Reporting of Certain Health and Welfare Benefit Plan Transactions*, would address issues related to employee health and welfare benefit plans that were not prevalent when SOP 92-6 was issued, including cost-sharing arrangements and amendments of plans to reduce benefits.

**Current development and plans.** At its April 1996 meeting, AcSEC voted to expose a draft SOP, subject to FASB clearance. The FASB discussed cost-sharing and benefits-reduction arrangements in September 1996 but did not clear the proposed conclusions. An SOP containing revised conclusions on that issue has been drafted by the Employee Benefit Plans Committee, and will be discussed at the January 1999 AcSEC meeting.

**Description and background.** The second SOP, *Accounting and Reporting of 401(h) Features of Defined Benefit Pension Plans*, would address the accounting for and disclosure of features of defined benefit pension plans, provided pursuant to section 401(h) of the Internal Revenue Code. That section allows sponsors of defined benefit pension plans to fund a portion of their postretirement medical obligations related to their health and welfare benefit plans through their defined benefit pension plans. The project would provide guidance for reporting by both defined benefit pension plans and health and welfare benefit plans.

**Current developments and plans.** FASB cleared the proposed exposure draft in March 1998 and it was released for comment on September 9, 1998. The comment period ended December 9, 1998, and the comments will be discussed at the January 1999 AcSEC meeting.

**Description and background.** The third SOP, *Accounting and Reporting for Certain Employee Benefit Plan Investments and Other Disclosure Matters*, would eliminate the requirement for defined contribution pension plans to report separate investment fund option information as required by PB 12.

**Current developments and plans.** AcSEC approved the draft SOP at its July 1998 meeting pending certain revisions. Discussion with the FASB for purposes of clearance for exposure is expected in the first quarter of 1999.

Staff: Wendy Frederick

#### **Financial Institutions: Banks, Credit Unions, Finance Companies, and Savings Institutions**

**Description and background.** AcSEC is undertaking an SOP project to reconcile the specialized accounting and financial reporting guidance established in the existing Guides *Banks and Savings Institutions*, *Audits of Credit Unions*, and *Audits of Finance Companies*. The final provisions would be incorporated in a final combined Guide, *Financial Institutions: Banks, Credit Unions, Finance Companies, and Savings Institutions*.

The proposed SOP eliminates differences in accounting and disclosure established by the respective Guides, and carries forward accounting guidance for transactions determined to be unique to certain financial institutions. Some of the more important issues being considered by AcSEC and the task force are as follows:

Mortgage companies and corporate credit unions will be explicitly included within the scope of the combined Guide. Regulatory capital disclosure requirements will also be added.

Banks and thrifts are presently required to disclose information about their regulatory capital requirements. Under the proposed SOP, credit unions will be required to disclose similar information.

Credit unions report amounts placed in their deposit insurance fund as an asset if such amounts are fully refundable, due to unique legal and operational aspects of the credit union share insurance fund. Banks and thrifts expense payments to their deposit insurance fund as incurred. Under the proposed SOP, both practices are expected to be preserved.

Finance companies record purchases and sales of securities on the settlement date, whereas banks, thrifts, and credit unions follow trade date accounting. Under the proposed SOP, finance companies will follow trade date accounting.

FASB Statement Nos. 114 and 118 address loan impairment measurement and disclosure requirements, but do not specify how to recognize income on impaired loans. The Guide for finance companies gives specific guidance on the recognition of interest income on impaired loans. Under the proposed SOP, such guidance will be eliminated.

Under the proposed SOP, certain disclosures for credit unions will be eliminated. These disclosures in the Guide for credit unions include, for example, additional information about repurchase agreements, servicing assets, and deposit liabilities.

**Current developments and plans.** AcSEC began deliberations on this project at its September 1998 meeting, and cleared the exposure draft of the proposed SOP at its December 1998 meeting. Discussion with the FASB for purposes of clearance for exposure is expected late in the first quarter of 1999.

Staff: Brad Davidson

#### **Mass Tort Exposures of Insurance Enterprises**

**Description and background.** AcSEC added this project to its agenda in 1996 in response to a request from the Insurance Companies Committee for a project to address diversity in practice in the recognition and measurement of liabilities for mass tort exposures of insurance enterprises.

*Continued on page 7*

This proposed SOP would—

- Include guidance on specific accounting issues that are present in the recognition of the various components of liabilities for mass tort exposures, including environmental and asbestos claims, in the financial statements.
- Address how the various components of mass tort exposure liabilities are measured.
- Include an educational discussion of the various methodologies and assumptions that are used to estimate mass tort exposure liabilities.
- Specify the disclosures to be provided in the notes to the financial statements for insurance enterprises.

**Current developments and plans.** AcSEC discussed a draft SOP at its December 1998 meeting. AcSEC members questioned the extent of improvement in practice that would result from the draft SOP. Some suggested that a Practice Bulletin (PB) or other publication would be appropriate. A redrafted document will be reviewed at a future AcSEC meeting to determine whether an SOP or PB is appropriate.

Staff: Fred Gill

## Motion Pictures

**Description and background.** This project was undertaken by AcSEC at the request of the FASB.

Since the issuance in 1981 of FASB Statement No. 53, *Financial Reporting by Distributors and Producers of Motion Picture Films*, the industry has undergone substantial changes. For instance, new forms of distribution such as videocassettes, cable television, and pay-per-view television have been introduced or have increased markedly in significance. Additionally, foreign markets have increased in significance.

**Current developments and plans.** The exposure draft was issued October 16, 1998 and comments were due by January 18, 1999.

Significant provisions of the proposed SOP are:

- Revenue should be recognized when all of a number of conditions are met, including:
  - Persuasive evidence of a sale or licensing arrangement with a customer exists.
  - The film is complete and, in accordance with the terms of the arrangement, either has been delivered or is available to be delivered.
  - The license period of the arrangement has begun and the customer can begin its exploitation or exhibition.

—The gross revenue is fixed or determinable.

—Collection is reasonably assured.

- The proposed SOP would also establish criteria for recognizing revenue from licensing arrangements.
- The costs of producing a film and bringing that film to market consist of production costs, exploitation costs, and participation costs.

—The present value of participation costs should be accrued when their payment is probable, which is usually determined when the film has been released. Entities should recognize an asset as part of film costs for the initial amount of the participation liability.

—Production costs and capitalized participation costs should be amortized using the individual-film-forecast-computation method, which requires estimating ultimate gross revenues. Ultimate gross revenues are limited to revenues expected to be received within 10 years of the film's initial release and are subject to other limitations. Amortization should begin when a film is released and revenues from that film are recognized.

—Prerelease and early release exploitation costs incurred on a territory-by-territory basis in the theatrical market should be capitalized and amortized over the expected period of exploitation of the film in that theatrical market and territory, not to exceed three months from release date. After the period leading up to the theatrical release of a film in a territory and the initial three-month period, all exploitation costs should be expensed as incurred. Exploitation costs incurred in connection with the release of a film in markets other than the theatrical market should be expensed as incurred.

- Unamortized film costs should be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the film may not be recoverable, in accordance with FASB Statement No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*.
- Certain disclosures should be made in the financial statements or notes thereto.

This SOP would be effective for financial statements for fiscal years beginning after December 15, 1999, with earlier application encouraged.

Staff: Dan Noll

Continued on page 8



## Nontraditional Long-Duration Contracts

**Description and background.** In February 1998, the FASB cleared a prospectus for the development of an SOP on accounting by insurance companies for certain nontraditional long-duration contracts and for separate accounts. The SOP will address the classification and valuation of liabilities as well as disclosures for nontraditional annuity and life insurance contracts issued by insurance enterprises. The AICPA Insurance Companies Committee identified this project because of the growing trend in insurers offering such contracts.

**Current developments and plans.** AcSEC held an informational discussion on this project in September 1998. AcSEC is scheduled to discuss, at its January 1999 meeting, tentative conclusions reached by the task force on accounting for separate accounts.

Staff: Elaine Lehnert

## Real Estate Time-Sharing Transactions

**Description and background.** AcSEC added this project to its agenda at the request of the Real Estate Committee. Because of a lack of guidance specific to real estate time-sharing transactions, diversity has arisen in practice. The SOP would attempt to reduce the diversity.

Issues to be addressed in this proposed SOP include:

- Which revenue recognition method should be used?
- How should allowances for uncollectible receivables be determined?
- What kinds of selling costs may be deferred?

**Current developments and plans.** At its October 1998 meeting, AcSEC directed the task force to develop an accounting model for time-sharing transactions that begins with the retail land sales model of FASB Statement No. 66, *Accounting for Sales of Real Estate*. AcSEC will consider asking the FASB to amend Statement 66 or other GAAP, as needed, to accommodate this model. The task force was also asked to address why time-sharing arrangements should not be accounted for as leases and to clarify the effect of any continuing involvement on the part of the seller, particularly when the time-sharing arrangement involves an exchange program.

AcSEC also determined that, for sales accounted for using a method other than full accrual, only incremental direct selling costs associated with successful sales efforts should be deferred based on a narrow interpretation of paragraph 18 of FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects*; all other selling and marketing costs should be expensed. Selling and marketing costs are to be excluded from the costs used in the calculation of revenue to be recognized under the percentage-of-completion method of Statement 66.

The task force was also asked to develop criteria for differentiating incidental operations (as defined in Statement 67) from non-incidental

operations, and for the appropriate accounting for time-sharing interests as inventory or fixed assets.

Staff: Marc Simon

## Interests in Unconsolidated Real Estate Investments

**Description and background.** This proposed SOP would supersede portions of SOP 78-9, *Accounting for Investments in Real Estate Ventures*. AcSEC added this project to its agenda in 1991 in response to inconsistent practice, especially in the area of loss recognition, and a lack of guidance on reporting on unincorporated entities.

**Current development and plans.** In December 1998, AcSEC decided that the SOP would benefit from a "fresh-start" rewrite to make it more concise and clearer to financial statement preparers. A small working group will be formed for this purpose. AcSEC determined that a number of the key conclusions of the most recent draft of the SOP would be retained, among which are the requirement that all unconsolidated real estate partnership investments follow equity method accounting, the use of the hypothetical-liquidation-at-book-value method, inclusion of investments in real estate corporations and corporate joint ventures in the scope of the SOP provided an investor has the ability to significantly influence the investee's operating or financial decisions, and accrual of losses by an investor up to its investment exposure and obligations.

A revised timetable has not yet been established.

Staff: Marc Simon

## Real Estate Cost Capitalization

**Description and background.** An SOP titled *Capitalization of Costs in Real Estate Assets Not Within the Scope of FASB Statement No. 67* will be developed by a task force of AcSEC to address accounting and disclosure issues related to the determination of which costs related to real estate assets should be capitalized as improvements or expensed as repairs and maintenance.

Diversity in practice regarding the capitalization of costs for improvements, replacements, betterments, additions (and terms synonymous to these such as redevelopments, refurbishments, renovations, and rehabilitations), and repairs and maintenance is one of the most prevalent accounting problems in the real estate industry at this time. The SEC has also expressed concerns over this area of accounting. Inconsistency has been observed in analogizing to FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects*, in accounting for real estate assets not covered under its scope.

**Current developments and plans.** On January 6, 1999, the FASB did not object to AcSEC proceeding with the project. Establishment of a task force is in process.

Staff: Marc Simon ♦

## AUDIT AND ACCOUNTING GUIDE PROJECTS IN PROCESS

AICPA Audit and Accounting Guides (Guides) point out guidance in other authoritative literature that preparers and auditors of financial statements of entities covered by those Guides should be aware of, and they often explain or illustrate such guidance. In addition, Guides often establish guidance on accounting issues not addressed in other authoritative literature.

Guidance in AICPA Guides that is based on other authoritative accounting and auditing literature is continually updated for “conforming changes” — changes in the authoritative literature upon which the guidance is based. In addition, Guides are revised completely when a need arises.

**Financial Institutions: Banks, Credit Unions, Finance Companies, and Savings Institutions** AcSEC is undertaking an SOP project (see page 6) to reconcile the specialized accounting and financial reporting guidance established in the existing Guides, *Banks and Savings Institutions*, *Audits of Credit Unions*, and *Audits of Finance Companies*. The final provisions of the SOP will be incorporated as conforming changes in a new combined Guide, *Financial Institutions: Banks, Credit Unions, Finance Companies, and Savings Institutions*.

**Life and Health Insurance Entities.** See page 2.

**Investment Companies.** See page 2.

## OTHER AcSEC ACTIVITIES

At its September 1998 meeting, AcSEC approved a comment letter on the FASB exposure draft, *Transfers of Assets Involving a Not-for-Profit Organization That Raises or Holds Contributions for Others*. AcSEC also did not object to a comment letter on the GASB’s proposed Technical Bulletin, *Disclosures about Year 2000 Resources Committed*. In addition, AcSEC discussed a comment letter on the IASC’s proposed standard, *Financial Instruments: Recognition and Measurement*.

## POTENTIAL FUTURE AcSEC PROJECTS

Prospectuses for the following projects have been approved by AcSEC’s Planning Subcommittee and are subject to FASB approval.

**Investment Companies Guide Scope SOP** In December 1998, AcSEC’s Planning Subcommittee approved a prospectus for a project to develop an SOP to address the scope of the AICPA Audit and Accounting Guide *Audits of Investment Companies*, issued in 1987 as updated only for conforming changes, and the 1998 exposure draft revising that Guide. The scope provisions of the exposure draft are unchanged from the current Guide, and FASB at its July 1998 meeting expressed concern that the scope of the proposed Guide may not be clear. This project will address whether more specific attributes of an investment company can be identified to

determine if an entity is within the scope of the Guide. The prospectus is expected to be discussed by the FASB in the first quarter of 1999.

**Allowance for Loan Losses SOP** In December 1998, AcSEC’s Planning Subcommittee approved a project to provide guidance related to identifying the appropriate point for loan loss accruals. The SEC recently expressed concerns about this area of accounting. The focus of the project will be on financial institutions and the lending process and identifying the event that gives rise to an accruable loss. The project is expected to expand upon relevant guidance in the AICPA Audit and Accounting Guide *Banks and Savings Institutions* and FASB Statement No. 5, *Accounting for Contingencies*.

**Mutual Company Reorganization SOP** In October 1998, AcSEC’s Planning Subcommittee approved a prospectus to develop an SOP titled *Accounting by Insurance Enterprises for Demutualizations and Formations of Mutual Insurance Holding Companies*. The proposed SOP will address the accounting for the formation of a mutual insurance holding company and demutualization accounting by insurance enterprises.

### Upcoming AcSEC Meetings

AcSEC meetings are open to the public.

January 28–29, 1999	San Diego, CA
March 9–10, 1999	New York
April 28–29, 1999	New York
June 15–16, 1999	New York

### AcSEC on AICPA Web Site

Look for information about AcSEC activities on the AICPA web site, “AICPA Online.” The AICPA web site address is: <http://www.aicpa.org>, and the area containing information pertaining to AcSEC activities is entitled “Accounting Standards Team.” This area can be accessed by clicking in the “choose a topic” section underneath “Information Solutions,” selecting “Accounting/Financial Reporting,” and clicking on “Go.” To view minutes of recent AcSEC meetings, click next on “Technical Status Updates” and then “Highlights of Recent AcSEC Meetings.”

## Comments or Suggestions?

We would welcome any comments or suggestions you may have concerning this publication. Write to Marc Simon at AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775, fax to 212-596-6064, or e-mail to [msimon@aicpa.org](mailto:msimon@aicpa.org).

## STAFF CONTACTS

Elizabeth Fender, Director	(212) 596-6159
Brad Davidson	(202) 434-4269
Wendy Frederick	(202) 434-9211
Frederick Gill	(212) 596-6012
Daniel Noll	(212) 596-6168
Elaine Lehnert	(212) 596-6160
Marc Simon	(212) 596-6161
Joel Tanenbaum	(212) 596-6164
Sheila Yu	(212) 596-6163

American Institute of Certified Public Accountants  
1211 Avenue of the Americas  
New York, NY 10036-8775

