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AcSEC UPDATE

A publication of the Accounting Standards Executive Committee and the Accounting Standards Team of the AICPA

AICPA

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

AcSEC UPDATE EXPANDS

Beginning with this issue, *AcSEC Update* will include information not only on activities of AcSEC but also on relevant activities of the Accounting Standards Team of the AICPA. The Accounting Standards Team provides staff support for AcSEC and many of the AICPA's technical industry committees and task forces. These committees and task forces work on the projects on AcSEC's agenda (see page 3), as well as other projects related to certain specialized industries and specific narrow topics.

This issue also includes a supplemental section *Facts About AcSEC*. This supplement describes the purpose of AcSEC, details the standards setting process for AcSEC Statements of Position, and provides information on the current members of AcSEC. *Facts About AcSEC* will be revised as a supplement on a periodic basis, including when the AcSEC membership changes on October 1 of each year. ❖

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*, which was issued in 1972 and updated only for conforming changes. AcSEC discussed the comment letters received on the exposure draft at its March 1999 meeting. AcSEC voted to issue a final Guide to reflect AcSEC's consideration of the comment letters, subject to clearance by the chair of AcSEC, a subcommittee of AcSEC, and the FASB.

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), which comprise 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 proposed 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.

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Recent AcSEC Activities *continued*

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 Investment Companies* which was issued in 1987 and 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 on reporting complex capital structures. The comment deadline was December 22, 1998. AcSEC is scheduled to discuss the comment letters at its April 1999 meeting.

Discounts Related to Credit Quality. On December 30, 1998, AcSEC issued an exposure draft of a proposed SOP *Accounting for Discounts Related to Credit Quality*. Comments are due by April 29, 1999. See page 4 for details on the project.

Motion Pictures. In March 1999, AcSEC had its first discussion of the major points raised in the comment letters received on the October 16, 1998 exposure draft SOP. AcSEC plans to complete this discussion at its April 1999 meeting and plans to review a draft of a final SOP at its July 1999 meeting. See page 6 for details on the project.

Employee Benefit Plans. At its January 1999 meeting, AcSEC cleared for exposure, pending certain revisions, the draft SOP *Accounting and Reporting of Certain Health and Welfare Benefit Plan Transactions*. The revised draft is expected to be sent to FASB during the second quarter of 1999. At this same meeting AcSEC cleared for final issuance, pending certain revisions, the SOP *Accounting and Reporting of 401(h) Features of Defined Benefit Pension Plans*. Pending clearance by FASB, the final SOP is expected to be issued during the second quarter of 1999. In February 1999, FASB cleared for exposure, pending certain revisions, the draft SOP *Accounting and Reporting for Certain Employee Benefit Plan Investments and Other Disclosure Matters*. An exposure draft is expected in the second quarter of 1999. See page 5 for details on these projects. ❖

EFFECTIVE DATES

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

Editor: **Marc Simon**
Administrative Editor: **Sharon Macey**

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

AcSEC AGENDA PROJECTS

As of March 31, 1999	1999 1Q	1999 2Q	1999 3Q	1999 4Q	2000 1Q
General Applicability					
Managed Care — SOP (page 4)					E
Lending Institutions					
Discounts Related to Credit Quality — SOP (page 4)					F
Banks and Savings Institutions, Credit Unions, and Finance Companies — SOP (page 5)			E		
Employee Benefit Plans					
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	F		
Investment Industry					
Investment Companies — Guide (page 2)				F	
Scope Clarification — Investment Companies Guide (page 8)					
Insurance Industry					
Life and Health Insurance Entities — Guide (page 1)			F		
Mass Tort Exposures — SOP (page 6)					
Nontraditional Contracts — SOP (page 6)				E	
Mutual Company Reorganizations — SOP (page 8)				E	
Motion Picture Industry					
Motion Pictures — SOP (page 6)				F	
Real Estate Industry					
Real Estate Investments — SOP (page 7)					
Real Estate Time-Sharing Transactions — SOP (page 7)				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, *Amortization of Discounts on Certain Acquired Loans*, 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 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 No. 114, *Accounting by Creditors for Impairment of a Loan*, and FASB Statement No. 118, *Accounting by Creditors for Impairment of a Loan — Income Recognition and Disclosures*. 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, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, 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

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 March 1999 meeting, AcSEC discussed key issues in the proposed SOP and agreed that it should continue to pursue a revenue and expense model given an IBNR model that assumes that liabilities should be accrued for all costs that are both probable (through the contract period) and reasonably estimable based on known events. AcSEC asked the task force to further explore a model that reports revenues and expenses consistent with current practice (revenue is reported ratably over the contract period, and expenses are reported as services are rendered and as the entity is otherwise obligated under the terms of the contract), and that reports an IBNR liability for all costs that are both probable and reasonably estimable based on known events through the contract period.

In addition, AcSEC asked the task force to explore other issues related to that IBNR model, such as (a) the operationality of identifying and measuring costs that are both probable (through the

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Facts About AcSEC

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Purpose of AcSEC

The Accounting Standards Executive Committee (AcSEC) is the senior technical committee at the AICPA authorized to set accounting standards and to speak for the Institute on accounting matters. In carrying out its standards-setting and communications activities, AcSEC maintains liaison with the Financial Accounting Standards Board (FASB), the Governmental Accounting Standards Board (GASB), the Securities and Exchange Commission (SEC), and the International Accounting Standards Committee (IASC). The accounting standards that AcSEC issues are prepared largely through the work of AICPA industry committees and task forces. The industry committees include Banking and Savings Institutions, Credit Unions, Employee Benefit Plans, Health Care, Insurance Companies, Investment Companies, Not-for-Profit Organizations, Public Utilities, Real Estate, and Stockbrokerage and Investment Banking.

The SEC, established in 1934, has statutory authority to set accounting standards, but has looked to the accounting profession to establish generally accepted accounting principles (GAAP) in the United States. FASB, an independent not-for-profit organization established in 1973, is the primary private-sector standards setter. As such, it establishes the highest level of accounting principles, Level A GAAP. The AICPA's AcSEC works closely with the FASB to establish consistent accounting standards in the United States. AcSEC Statements of Position (SOPs) are established as the next highest level of accounting principles, Level B GAAP. AcSEC also issues industry audit and accounting guides, practice bulletins, issues papers, and comment letters on other standards setters' proposed guidance. AcSEC's standards-setting activities are often industry-specific or narrow in their scope, unlike the majority of FASB's projects, which are broader in scope.

Meetings

AcSEC generally meets eight times a year. Meetings are open to the public. Immediately preceding each meeting is a nonpublic meeting of AcSEC's Planning Subcommittee (PSC). The PSC determines AcSEC's agenda, sets priorities for AcSEC projects, and monitors the progress of the projects. The PSC also assists the Chair of AcSEC with certain administrative and technical responsibilities.

The Standards Setting Process for AcSEC Statements of Position

AcSEC's standards setting process for its SOPs is outlined below:

- An accounting or reporting issue requiring guidance, typically due to an emerging problem or diversity in practice, is either identified by AcSEC or brought to AcSEC's attention. An appropriate standing AICPA industry committee or an AICPA task force drafts a prospectus for a project to address the practice problem and presents it to the PSC for approval to undertake the project. The prospectus addresses the nature and pervasiveness of the problem, the technical feasibility of developing an operational solution, alternative solutions, and practical consequences that may result from those solutions. In preparing the prospectus the committee or task force looks to address and meet certain clearance criteria used by the FASB, namely, that the project does not amend or conflict with existing GAAP, that it should result in an improvement in practice, that there is a definite need for the project, and that the benefits of the project are expected to exceed its costs. If the project is approved by the PSC, the prospectus is discussed in a public meeting with the FASB. FASB requires that 5 of FASB's 7 members not object to the project as presented in the prospectus before it is added to AcSEC's agenda.

- The AICPA committee or task force develops a proposed Statement of Position and brings it to AcSEC for approval to expose the proposed SOP to the public for comment. AcSEC may discuss the project over the course of several meetings, may hold informational or educational sessions for its members, and may request that the task force or industry committee make substantial revisions to the draft. Approval of the proposed SOP for exposure requires at least a two-thirds vote of AcSEC members.
- At a public FASB meeting, representatives of AcSEC and the committee or task force then discuss the proposed SOP with the FASB. FASB's clearance criteria and voting process for exposure of the proposed SOP are similar to those for the prospectus. FASB may also suggest changes. Once FASB clearance is obtained, an exposure draft is issued by the AICPA.
- AcSEC and the AICPA committee or task force review all comment letters received. The task force may recommend changes in the document based on the comments received, and AcSEC decides which of those changes should be made to the proposed SOP. FASB also reviews the comment letters.
- AcSEC, which may discuss the proposed revisions over the course of several meetings, indicates revisions required before approving the document for final issuance. Approval of an SOP requires at least a two-thirds vote of AcSEC members.
- FASB discusses the revised SOP with the AcSEC and task force chairs in a public FASB meeting. FASB's clearance criteria and voting process for issuance are similar to those for the prospectus and exposure draft. The FASB may request or require that certain revisions be made in deciding whether to clear the document for issuance.
- A similar process exists when AcSEC clears documents through the GASB. A similar but somewhat less extensive process is used for issuing practice bulletins, as practice bulletins do not require public exposure.

Sometimes the nature of an accounting or reporting issue is such that AcSEC considers it more appropriate that it be considered by the FASB or FASB's Emerging Issues Task Force (EITF). In such cases, AcSEC will refer the issue to FASB or EITF. The AcSEC chair is a member of the EITF's agenda committee and is a non-voting observer at EITF meetings.

Members of AcSEC

AcSEC is composed of 15 volunteer members, representative of industry, academia, analysts, and both national and regional public accounting firms. All AcSEC members are CPAs and members of the AICPA. As of October 1, 1998, the members are:

Dave Kaplan, *Chair*	(PricewaterhouseCoopers LLP; Stamford, CT)
Al Adkins	(USX Corporation; Pittsburgh, PA)
Mark Bielstein	(KPMG Peat Marwick LLP; New York, NY)
Cassandra Camp	(Carlin, Charron & Rosen LLP; Worcester, MA)
Joe Cappalonga	(Deloitte & Touche LLP; Wilton, CT)
Jack Ciesielski	(R.G. Associates; Baltimore, MD)
Bob Dale	(Purvis, Gray and Company; Gainesville, FL)
Joe Graziano	(Grant Thornton LLP; New York, NY)
Ray Krause	(McGladrey & Pullen, LLP; Bloomington, MN)
Lou Matusiak	(Olive LLP; Indianapolis, IN)
David Morris	(The Chase Manhattan Bank; New York, NY)
Ben Neuhausen	(Arthur Andersen LLP; Chicago, IL)
Paula Panik	(The Travelers Insurance Companies; Hartford, CT)
Mark Sever	(Ernst & Young LLP; Chicago, IL)
Mary Stone	(University of Alabama; Tuscaloosa, AL)

Each member is appointed for one year with three years being the maximum term; however, certain members have been on AcSEC for longer periods.

Additional Information

AcSEC Update: *AcSEC Update* is the newsletter of AcSEC and is published three to four times a year. It provides information about recently issued AcSEC pronouncements and current AcSEC projects. For further information, contact Marc Simon by e-mail at *msimon@aicpa.org*.

AICPA Web Site: Information about AcSEC activities, including exposure drafts, appears 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" and selecting "Accounting/Financial Reporting."

AcSEC Pronouncements: To order copies of AcSEC pronouncements — write to 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) and ask for Operator NQ. Orders for exposure drafts (one copy is free) must be written or faxed if not obtained from the web site.

Members of AcSEC — Biographical Information

Dave Kaplan (AcSEC Chair) is a partner in PricewaterhouseCoopers LLP and co-director of the firm's National Accounting Consulting Services Group. He is the AcSEC observer to the FASB's Emerging Issues Task Force and a member of the Steering Committee of the FASB's Business Reporting Research Project. Mr. Kaplan has been a member of AcSEC since 1995. Prior to joining the National Office of PricewaterhouseCoopers in 1995, he was a client service partner and the firm's Northeast region risk management partner. Mr. Kaplan joined the firm in 1976 and was admitted to the partnership in 1987. He holds BS and MSBA degrees in Accounting from the University of Massachusetts.

Al Adkins is Assistant Comptroller for USX Corporation in Pittsburgh, PA. In over twenty years with USX, Mr. Adkins has held accounting, purchasing, finance, and tax positions within other areas of USX. In late 1997, Mr. Adkins assumed his current position with USX and relocated to Pittsburgh, PA. He holds a BS degree in Accounting from Marshall University in Huntington, WV.

Mark Bielstein is a partner with KPMG Peat Marwick LLP in the firm's Department of Professional Practice — Assurance & Advisory Services in New York. He has been with KPMG for 21 years. Prior to joining the firm's National Office, Mark was an assurance partner in the San Antonio office where he served clients in a variety of industries. Mark holds a BBA from Baylor University.

Cassandra Camp is a partner at Carlin, Charron & Rosen LLP, headquartered in Worcester, Massachusetts. The firm is the second largest non-national firm in Massachusetts, with 5 offices and approximately 145 employees. Ms. Camp chairs the firm's audit and accounting committee, with responsibility for setting firm policy regarding audit procedures and implementation of new auditing and accounting standards. Previously, Ms. Camp was an audit manager at Coopers & Lybrand and the director of cost accounting for Teradyne, both in Boston. She holds both undergraduate and graduate degrees in Accounting from the University of Texas. She has served on the AICPA Accounting and Review Services Committee and the PCPS Technical Issues Committee.

Joe Cappalonga is the National Director of Accounting Services of Deloitte & Touche LLP. He has been an AcSEC member since 1994. Prior to joining his National Office in 1993, Mr. Cappalonga was the Audit Partner-In-Charge of the firm's Philadelphia area practice. He holds a BS degree from the United States Naval Academy and an MBA from the University of Pennsylvania, Wharton Graduate School.

Jack Ciesielski is the owner of R.G. Associates, Inc., an investment research and management firm which publishes *The Analyst's Accounting Observer*, an accounting advisory service for security analysts. Before founding R.G. Associates in 1992, he spent nearly seven years as a security analyst with the Legg Mason Value Trust. He has performed various stints in the accounting profession as an auditor with Coopers & Lybrand, an internal auditor with Black & Decker, and an educator at the University of Maryland. He holds BA and MSF degrees from Loyola College in Baltimore.

Bob Dale is an audit partner in the Gainesville, Florida office of Purvis, Gray and Company. He joined the firm in 1972 and was appointed Partner-in-Charge of the firm's audit department in 1989. He is a graduate of the University of Florida with a degree in Accounting. From 1990 to 1996 Mr. Dale served on the AICPA's Technical Issues Committee, serving as committee chair from 1993 to 1996.

Joe Graziano is the national director of SEC and financial reporting for Grant Thornton LLP. Prior to transferring to the National Office, Mr. Graziano was an assurance partner in its New York office. He holds a BBA from Bernard M. Baruch College and an MBA from St. John's University.

Ray Krause is the National Director of Accounting in the National Office of Audit and Accounting of McGladrey & Pullen, LLP. Mr. Krause is a member of the Emerging Issues Task Force of the FASB and the Financial Accounting Standards Advisory Council. Mr. Krause graduated with Scholastic Honors from Northern Illinois University.

Lou Matusiak is the Report Review Partner of Olive LLP. In this capacity he reviews and approves all assurance reports that are signed with the firm's name. He also is the firm's senior technical consultant for accounting matters. Prior to accepting this position, Lou was an audit partner in the firm's Decatur, Illinois office, specializing in financial institutions. He holds a BA from Southern Illinois University.

David Morris is Financial Director of Corporate Accounting Policies of The Chase Manhattan Bank. Before joining Chase in 1984, Mr. Morris was a senior audit manager with Price Waterhouse. He holds a BS from Case Institute of Technology and an MBA from the University of Michigan. He currently is Chairman of both the Technical Committee of International Association of Financial Executives Institutes (IAFEI) and the Accounting Committee of International Swaps and Derivatives Association (ISDA).

Ben Neuhausen is a partner with the Professional Standards Group of Arthur Andersen LLP. His principal areas of specialization include compensation and employee benefits, financial instruments, insurance and leasing. Before joining the Professional Standards Group, Mr. Neuhausen worked in the audit practice of Arthur Andersen in New York with clients in a variety of industries. From 1979 to 1981, Mr. Neuhausen was a Practice Fellow at the FASB. He holds a BA in Economics from Michigan State University and an MBA in Accounting from New York University.

Paula Panik is vice president, accounting policy and finance at Travelers Property Casualty Corp. and Travelers Life and Annuity, members of Citigroup. Prior to joining Travelers, Ms. Panik was an audit manager at Price Waterhouse. Before joining Price Waterhouse, she was chairman of the Department of Economics and Business and of the Division of Social Sciences at St. Joseph College, West Hartford, Connecticut. Ms. Panik holds a BS from St. Bonaventure University, and MS degrees from Boston College and the University of Hartford.

Mark Sever is a partner in Ernst & Young's National Office where he serves as a Professional Practice Director for the Lake Michigan Area office. In his career at E & Y, Mark has served a variety of clients in the financial services, insurance and manufacturing industries. Mark was a Practice Fellow with the FASB and has served on the AICPA's Information Retrieval Task Force and the Financial Instruments Task Force. Mark is a graduate of the University of Notre Dame.

Mary Stone is an Ernst & Young Professor in the Culverhouse School of Accounting at the University of Alabama. Dr. Stone teaches undergraduate, graduate, and CPE courses. Her research is published in academic and professional journals. Dr. Stone earned her bachelors and masters degrees from the University of Central Florida and her Ph.D. in accounting from the University of Illinois at Urbana-Champaign.

contract period) and reasonably estimable based on known events and (b) whether the balance sheet debit that results under that model meets the definition of an asset. An exposure draft is expected in the first quarter of 2000.

Staff: Joel Tanenbaum

Employee Benefit Plans

There are three proposed SOPs that 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*.

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 January 1999 meeting, AcSEC cleared the draft SOP for exposure pending certain revisions. The revised draft is expected to be sent to FASB during the second quarter of 1999.

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 that are permitted under 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. At its January 1999 meeting, AcSEC cleared the SOP for final issuance pending certain revisions. Pending clearance by FASB, the final SOP is expected to be issued during the second quarter of 1999.

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. FASB cleared the draft SOP for exposure in February 1999 pending certain revisions. An exposure draft is expected in the second quarter of 1999.

Staff: Wendy Frederick

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

Description and background. This SOP project is 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 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 in the second quarter of 1999.

Staff: Brad Davidson

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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.

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 may be more 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. In March 1999, AcSEC had its first discussion of the major points raised in the comment letters received on the October 16, 1998 exposure draft SOP. AcSEC plans to complete this discussion at its April 1999 meeting and plans to review a draft of a final SOP at its July 1999 meeting.

AcSEC indicated its preliminary positions on the following issues in the exposure draft:

Abandoned properties — AcSEC continues to support the proposed accounting.

Episodic television losses — AcSEC continues to support the proposed accounting, including the limitation on secondary market revenues.

Film changes after delivery — AcSEC supports a change to the exposure draft whereby significant changes to a film would be defined as those changes that are additive, which involves creation by entities of new or additional content after delivery. Changes such as dubbing and adding subtitles would therefore not be considered significant changes that preclude revenue recognition.

Participations and residuals — AcSEC supports a change to the exposure draft whereby participations and residuals would be accounted for under current practice, that is, costs should be accrued as revenue is earned.

Exploitation costs — AcSEC supports a change to the exposure draft whereby all exploitation costs would be accounted for under SOP 93-7, *Reporting on Advertising Costs*.

Transition — AcSEC supports extending the effective date one year, making the SOP effective for fiscal years beginning after December 15, 2000.

Staff: Dan Noll

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. At its January 1999 meeting, AcSEC tentatively concluded that separate accounts should be included in the financial statements of the insurance enterprise. AcSEC discussed criteria, proposed by the project's task force, that should be used to determine whether the assets and liabilities of separate accounts should be reported as a single line item on the respective sides of the balance sheet, referred to as "one-line" presentation. Contracts that satisfy all four of the following proposed criteria should be reported using the one-line method. The task force proposed to AcSEC that:

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- ◆ The assets reside in a legally recognized separate account.
- ◆ The contract holder, not the insurance enterprise, directs the allocation of amounts invested in the separate account among the available investment alternatives.
- ◆ The performance of the assets determines the value of the contract liabilities.
- ◆ The investment performance is not guaranteed by the insurance enterprise.

In addition, the task force proposed that arrangements that satisfy the first three criteria but not the fourth would also be reported using the one-line method, with any liability for the guarantee and related expense reported separately with all of the other liabilities of the insurance enterprise. AcSEC asked the task force to provide information about why each of these criteria are necessary and the implications of eliminating each one.

AcSEC also asked the task force to develop three models for display of separate accounts in the financial statements of insurance enterprises, and to discuss at its April 1999 meeting the benefits, drawbacks, impact on the balance sheet and income statement, and disclosure requirements of each model. The three models are as follows:

- ◆ Amend paragraphs 53 and 54 of FASB Statement No. 60, *Accounting and Reporting by Insurance Enterprises*, to eliminate the one-line presentation for all assets and liabilities of contracts offered through separate accounts.
- ◆ Allow only separate accounts without any type of guarantee to be presented as a one-line item on the balance sheet of an insurance enterprise.
- ◆ Allow separate accounts that are not fully guaranteed by the insurance enterprise to be presented as a one-line item on the balance sheet.

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 diversity in practice caused by a lack of guidance specific to real estate time-sharing transactions. The SOP would attempt to reduce the diversity.

Issues to be addressed in this proposed SOP include:

- ◆ Which profit 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 January 1999 meeting, AcSEC determined that (1) time-sharing transactions should be considered "real estate" for purposes of the SOP, (2) passage of non-reversionary title must be one of the criteria for recognizing a sale, and (3) a seller is not precluded from recognizing a sale solely because the property is not completed and available for occupancy.

AcSEC determined at a previous meeting 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 FASB Statement No. 66, *Accounting for Sales of Real Estate*.

At the April 1999 meeting, the task force will present to AcSEC its proposed model for time-sharing transactions. Although this model is based on the retail land sales model of Statement 66, it draws upon many of the fundamental principles of the other-than-retail-land-sales model of that Statement.

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. AcSEC determined that 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 investee losses by an investor up to its investment exposure and obligations.

A working group has been formed and has begun the rewriting process. The group expects to make a presentation at the June 1999 AcSEC meeting.

Staff: Marc Simon

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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.

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

Staff: Marc Simon

Mutual Company Reorganizations

Description and background. In February 1999, the FASB cleared a prospectus for the development of an SOP on accounting by insurance enterprises for demutualizations and formations of mutual insurance holding companies. The AICPA Insurance Companies Committee identified this project because of the growing trend for mutual insurers to form mutual holding companies or to demutualize.

Current developments and plans. At its April 1999 meeting, AcSEC is scheduled to hold an educational session and begin discussing issues and tentative conclusions reached by the task force.

Clarification of the Scope of the Investment Companies Guide

Description and background. In February 1999, the FASB 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*, which was issued in 1987 and 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 be unclear. 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.

Current developments and plans. A discussion of key issues is planned for the April 1999 AcSEC meeting.

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 and auditing 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 — See page 5.

Life and Health Insurance Entities — See page 1.

Investment Companies — See page 2.

OTHER AcSEC ACTIVITIES

At its January 1999 meeting, AcSEC —

- Approved a draft comment letter on the "G4+1" Invitation to Comment on Business Combinations.
- Met with representatives of the AICPA's Partnering for CPA Practice Success (PCPS) Technical Issues Committee to discuss various matters of mutual interest.

At its March 1999 meeting, AcSEC —

- Discussed a draft AICPA comment letter on the International Accounting Standards Committee's (IASC's) December 1998 discussion paper, *Shaping IASC for the Future*, and provided its views on the IASC's future structure and process.
- Met with representatives of the Association for Investment Management and Research and discussed communications with the analyst community, the scope of AcSEC projects, the IASC's future structure and process, and the business reporting model.

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. Exposure drafts may also be obtained through the AICPA web site; see "AcSEC ON AICPA WEB SITE" on page 9.

POTENTIAL FUTURE AcSEC PROJECT

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 focus of the project will be on financial institutions, the lending process, and identifying the situation at a reporting date 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 Nos. 5 and 114, *Accounting for Contingencies* and *Accounting by Creditors for Impairment of a Loan*, respectively. A task force has been formed to study the issue. The prospectus has not yet been approved by the FASB.

Upcoming AcSEC Meetings

AcSEC meetings are open to the public.

April 28–30, 1999	New York
June 16–18, 1999	New York
July 27–28, 1999	Colorado Springs, CO
September 14–15, 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." Or, to obtain a copy of an exposure draft, after clicking on "Go" click on "Technical Documents."

OTHER ACTIVITIES OF THE ACCOUNTING STANDARDS TEAM OF THE AICPA

International Accounting Standards Committee (IASC)

The AICPA, together with the Institute of Management Accountants (IMA), co-hosted the March 1999 meeting of the IASC in Washington, DC. This was the first IASC Board meeting that was open to public observation. A formal dinner welcoming the IASC members was hosted by the AICPA, IMA, the Association of Investment Management and Research, and the Financial Executives Institute.

As one of the founding members of the IASC, the AICPA has used its best efforts in supporting the IASC's work since 1973. The AICPA appointed former AcSEC Chair G. Michael Crooch of Arthur Andersen as its representative on the IASC and provides the technical adviser to the delegation (Liz Fender/Fred Gill).

The Board approved IAS 10 (revised), *Events After the Balance Sheet Date*, and discussed drafts of exposure drafts on agriculture and investment properties. Both drafts will be revised for further deliberation at the Board's next meeting in Warsaw, Poland, on June 29 to July 2, 1999.

Acquired In-Process Research and Development (IPR&D)

The Accounting Standards Team is working with a cross section of experts from industry, public accounting firms, the financial analyst community, and appraisal firms to identify best practices related to definitions, accounting, disclosures, valuation, and auditing of acquired IPR&D. An IPR&D task force has formed working groups for this purpose and expects to release its findings in 1999.

Technical Practice Aids

Staff of the Accounting Standards Team recently released two groups of nonauthoritative questions and answers (Q&As), commonly referred to as Technical Practice Aids (TPAs). The first group pertains to software revenue recognition, and the second to not-for-profit organizations. The TPAs have not been approved, disapproved, or otherwise acted upon by AcSEC or any other senior technical committee of the AICPA. They are not sources of established accounting principles as described in SAS No. 69, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles in the Independent Auditor's Report*.

The Q&As on software revenue recognition relate to SOP 97-2, *Software Revenue Recognition*. These may be viewed on the AICPA web site at *http://www.aicpa.org/members/div/acctstd/general/tpal.htm*. These Q&As, and the ones relating to not-for-profit organizations, will be included in the next update of the AICPA's *Technical Practice Aids*. AICPA members with questions on these TPAs should call the AICPA's Technical Hotline, which provides nonauthoritative guidance on accounting and attest issues, at (888) 777-7077.

Comments or Suggestions?

We welcome any comments or suggestions you may have concerning this publication. Please send to *msimon@aicpa.org*, fax to 212-596-6064, or write to Marc Simon at AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775.

STAFF CONTACTS

Elizabeth Fender, Director	efender@aicpa.org	(212) 596-6159
Brad Davidson	bdavidson@aicpa.org	(202) 434-9269
Wendy Frederick	wfrederick@aicpa.org	(202) 434-9211
Fred Gill	fgill@aicpa.org	(212) 596-6012
Dan Noll	dnoll@aicpa.org	(212) 596-6168
Elaine Lehnert	elehnert@aicpa.org	(212) 596-6160
Marc Simon	msimon@aicpa.org	(212) 596-6161
Joel Tanenbaum	jtanenbaum@aicpa.org	(212) 596-6164
Sheila Yu	syu@aicpa.org	(212) 596-6163

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