2013 A&A Update

TSTCI Finance/Accounting/ Commercial Conference

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ASU 2011-08 – Testing Goodwill for Impairment

- Objective of amendment is to simplify how entities test for impairment, allowing assessment of qualitative factors to determine whether it is "more likely than not" that the FV of the reporting unit is less than its carrying amount, as a basis for determining whether performance of the two-step approach is necessary

ASU 2011-08 – Testing Goodwill for Impairment

- "More likely than not" means more than a 50% likelihood
- Previous standards required, at least annually, comparison of FV of reporting unit to carrying amount, including goodwill
- If FV was less than carrying amount, step two measured "implied FV" of goodwill, compared to carrying amount of goodwill, to determine impairment loss
- Effective for years beginning after 12/15/11

ASU 2012-02 Testing Indefinite Lived Intangibles for Impairment

- Adopts basically the same impairment test for indefinite lived intangibles as is used for Goodwill
- Effective for years beginning after 9/15/12
- Factors to consider
  - Cost and financial performance
  - Legal, regulatory, contractual, & political factors
  - Changes in management or key personnel
  - Industry and market conditions
  - General economic conditions

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- Addresses concerns from users about lack of transparency regarding employers' participation in multiple employer pension plans (cost-sharing plans)
- Unique aspect of such plans is that assets contributed by one employer can be used to pay benefits to employees of another participating employer, since assets are not earmarked only for employees of the contributing employer (as in agent plan)

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- If a participating employer fails to contribute its required amounts, unfunded obligation may be passed on to remaining participating employers
- Likewise, if a participating employer withdraws from plan, withdrawing entity may be required to pay plan a final payment (the withdrawal liability)

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- Users requested additional disclosure to increase awareness of commitments and risks related to employers' participation
- Previous disclosures were limited to historical amounts contributed to the plan
- Amendments also require changes in disclosures of multiemployer plans that provide postretirement benefits other than pension ("other postretirement benefits")

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- Amendments do not apply to plans that maintain separate accounts for each employer, so that contributions provide benefits only to the employees of the contributing employer
- Amendments require employers who are subsidiaries participating in parent's single-employer plan and not-for profits that participate in their national organization's single-employer plan provide the name of the plan in which the employer participates

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- Amended disclosures include:
  - Significant multiemployer plans in which an employer participates, including plan names and <u>identifying numbers</u>
  - Level of employer's participation in significant multiemployer plans, including the employer's contributions made to plans and indication of whether employer's contributions represent more than 5% of total contributions made to plan by all contributing employers

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- Amended disclosures include:
  - Financial health of plans, including indication of funded status, whether funding improvement plans are pending or implemented, and whether plans has imposed surcharges on contributions
  - Nature of employer commitments to plans, including when collective-bargaining agreements that require contributions to significant plans are to expire and whether those agreements require minimum contributions to plans

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- Using the employer ID number, plan name, and (if applicable), plan numbers, users would be able to obtain additional information, including funded status of plans, from outside sources, such as plans annual Form 5500
- For other plans for which users are not able to obtain additional publicly available information outside employer's financial statements, additional disclosures are required

ASU 2011-09 – Disclosure about Employers' Participation in Multiemployer Plan

- Current guidance on recognition and measurement for employer's participation in multiemployer plan, which requires that employer recognize its required contribution to plan as pension or other postretirement benefit cost for period and recognize liability for any contributions due at reporting date remain unchanged
- Effective for periods ending after 12/15/12

Other Comprehensive Income (OCI) Presentation

- Beginning with calendar year 2012 financial statements, can no longer include OCI on Statement of Changes in Stockholders Equity
- Must either be a separate statement directly following income statement or combine with the statement of income

ASU 2013-02 Enhanced Disclosures Concerning Reclassifications out of Accumulated OCI

- Requires disclosure of reclassification adjustments for each separate component of OCI
- Presentation can be before or after tax
- Requires disclosure on face of income statement or in a footnote, the effect on specific line items in the income statement
    - If on face of statement, include parenthetically on income statement line item with tax effect on income tax line
    - If in a footnote, either before or after tax, indicate income statement line item by each OCI component

2013-02 Example 1 – Reclassification Adjustments by OCI Component

Entity XYZ
Notes to Financial Statements
Changes in Accumulated Other Comprehensive Income by Component [a]

For the Period Ended December 31, 201X

	Gains and Losses on Cash Flow Hedges	Unrealized Gains and Losses on Available-for-Sale Securities	Defined Benefit Pension Items	Foreign Currency Items	Total
Beginning balance	$ (1,200)	$ 1,000	$ (8,800)	$ 1,300	$ (7,700)
Other comprehensive income before reclassifications	3,000	2,500	(3,000)	1,000	3,500
Amounts reclassified from accumulated other comprehensive income	(750)	(1,500)	4,500	-	2,250
Net current-period other comprehensive income	2,250	1,000	1,500	1,000	5,750
Ending balance	$ 1,050	$ 2,000	$ (7,300)	$ 2,300	$ (1,950)

(a) All amounts are net of tax. Amounts in parentheses indicate debits.

2013-02 Example 2 – Income Statement Effect in Footnote

Entity XYZ
Notes to Financial Statements
Reclassifications Out of Accumulated Other Comprehensive Income [a]
For the Period Ended December 31, 201X

Details about Accumulated Other Comprehensive Income Components	Amount Reclassified from Accumulated Other Comprehensive Income	Affected Line Item in the Statement Where Net Income Is Presented
Gains and losses on cash flow hedges		
Interest rate contracts	$ 1,000	Interest income/(expense)
Credit derivatives	(500)	Other income/(expense)
Foreign exchange contracts	2,500	Sales/revenue
Commodity contracts	(2,000)	Cost of sales
	1,000	Total before tax
	(250)	Tax (expense) or benefit
	$ 750	Net of tax
Unrealized gains and losses on available-for-sale securities		
	$ 2,300	Realized gain/(loss) on sale of securities
	(285)	Impairment expense
Insignificant items	(15)	
	2,000	Total before tax
	(500)	Tax (expense) or benefit
	$ 1,500	Net of tax

2013-02 Example 2 – Income Statement Effect in Footnote

Amortization of defined benefit pension items			
Prior-service costs	$	(2,000) [b]	
Transition obligation		(2,500) [b]	
Actuarial gains/(losses)		(1,500) [b]	
		(6,000)	Total before tax
		1,500	Tax (expense) or benefit
	$	(4,500)	Net of tax
Total reclassifications for the period	$	(2,250)	Net of tax

(a) Amounts in parentheses indicate debits to profit/loss.

(b) These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see pension footnote for additional details).

2013-02 Example 3 – Income Statement Effect on Statement

Entity ABC
Statement of Income
For the Period Ended December 31, 201X

Revenues (includes $4,000 accumulated other comprehensive income reclassifications for net gains on cash flow hedges)	$	122,500
Expenses (includes ($1,000) accumulated other comprehensive income reclassifications for net losses on cash flow hedges)		(32,000)
Other gains and losses		5,000
Gain on sale of securities (includes $4,000 accumulated other comprehensive income reclassifications for unrealized net gains on available-for-sale securities)		4,000
Income from operations before tax		99,500
Income tax expense (includes ($1,750) income tax expense from reclassification items)		(24,875)
Net income	$	74,625

ASU 2013-02

- Effective for fiscal years beginning after December 15, 2003 with early adoption permitted.

ASU 2013-03 Fair Value Disclosures

- Clarifies that non-public entities are not required to disclose the level in which the fair value measure is categorized (Level 1, 2, or 3) for assets and liabilities not recognized at fair value in the balance sheet but for which disclosure of fair value is required

Exposure draft – Revenue from Contracts with Customers

- Issued in January 2012 (3rd ED); key area needed to converge with IFRS
- Proposed amendments seek to:
  - Remove inconsistencies and eliminate weaknesses in existing revenue recognition requirements
  - Provide more robust framework for addressing revenue issues
  - Improve comparability of practices across entities, industries, jurisdictions and capital markets

Exposure draft – Revenue from Contracts with Customers

- Effective date proposed will be no sooner than periods beginning on or after 1/1/15
- Early application will not be permitted, although IASB has decided to permit early application
- Will replace multiple deliverable and all other revenue recognition guidance.

Audit Issues

- Changed standard audit report to divide into six paragraphs versus three and contains subheadings
- Essentially says the same thing as the former opinion
- Financial statement preparation is no longer considered an attest service
- This would include preparation of financial statements in conjunction with an audit
- May eliminate internal control comments on financial statement preparation

Audit Issues

- New documentation requirements for non-attest services
- Must document:
  - services performed,
  - if there is a specific prohibition,
  - if the service will involve assuming management responsibilities,
  - threats to independence,
  - safeguards and their reduction of threats,

Audit Issues

- Must document:
  - <u>name of individual designated to oversee service,</u>
  - <u>skills, knowledge, and experience that allows the individual to effectively oversee and take responsibility,</u>
  - <u>entity's agreement to accept responsibility,</u>
  - <u>understanding of objectives and responsibilities</u>

Revisiting Impairments

- Required to consider need to recognize a loss whenever events or circumstances indicate the carrying amount may not be recoverable
  - Market value of assets significantly decrease
  - Adverse change in physical condition of asset or the way it is being used
  - Significant adverse change in legal factors or business climate (actions by regulators)

Revisiting Impairments

- Incurring costs to acquire asset that are significantly higher than originally planned
- Current period operating or cash flow losses along with history of such losses from using the asset accompanied by projections or forecast for continuing losses
- More likely than not expectation that asset will be sold or disposed of prior to end of its useful life

Revisiting Impairments

- First step is to estimate undiscounted future cash flows
- If cash flows equal or exceed carrying amount of asset, no impairment
- If carrying amount exceeds cash flow, calculate fair value and recognize impairment loss for excess of carrying amount over fair value
- Fair value is the new depreciable basis

Revisiting Impairments

- Calculating estimated future cash flows
  - Period should be the remaining life of the asset
  - Include receipts and disbursements associated with, and expected to arise as a direct result of, the use and eventual disposition of the asset
  - Exclude interest expense
  - Exclude allocated costs that would be incurred regardless of asset use
  - Include future capital expenditures to upgrade asset or assets

Revisiting Impairments

- Calculating fair value
  - Quoted market price in an active market for your asset
  - Quoted market price in active market for similar assets
  - Valuation techniques such as present value of future cash flows

Revisiting Impairments

- Potential Impairment Areas
  - Video – business is maturing to the point where impairment may need to be considered
  - Small wireless operations
  - Transport
  - Regulated telco operations depending upon legislative and regulatory actions

Revisiting Impairments

- In communications industry, impairment will rarely involve just one asset but will involve a business segment
- Consider contribution margin of business segment – fixed costs absorbed
- Impairments will probably be necessary when an entity has discontinued operations

Retirements

- Still not being made consistently
- Distorts depreciation expense
- Timing is not a choice, retirement should be made in period asset is removed from service
- Failure to report items removed from service to accounting seems to be the most frequent reason that retirements go unrecorded
- Physical inventory of COE to update CPRs may be needed
- Assets with significant movement, such as, set top boxes and other CPE create problems

Salvage

- Credits to accumulated depreciation that can be in the form of cash, materials returned to stock, or trade-ins
- In most cases, if causes over depreciation, reverse depreciation expense
- Most inventory write-offs should be recorded as reversal of salvage unless new equipment that has never been in service
- Avoid returning materials to stock if unlikely it will ever be reused

Advance Billing

- Advance bill items should be recorded as deferred revenue
- For customer billing, can exclude advance bill from AR recording
- Most customer billed items are in advance – local, unrated toll, internet, video
- Other advance billings – transport and FABS
- Some transport deferred revenue should be classified as a long-term liability if contract longer than 1 year

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