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Financial Accounting Standards Board
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Dear Ms. Bielstein:

The Accounting Standards Executive Committee (AcSEC) of the American Institute of Certified Public Accountants is pleased to offer its comments on the FASB's December 15, 2003, exposure draft, Accounting Changes and Error Corrections—a replacement of APB Opinion No. 20 and FASB Statement No. 3.

A majority of AcSEC members agree that the exposure draft's retrospective approach for voluntary changes in accounting principle will enhance the usefulness of financial statements and, in particular, result in improved comparability among periods. Those members who agree with the retrospective approach are nevertheless concerned about certain practical aspects of implementing that approach. Reasons some members do not agree with the retrospective approach include a possible negative effect on the credibility of financial statements and the possibility that the cost of retrospective application would act as a disincentive for reporting entities to adopt preferable accounting principles.

## Definition of "Impracticability"

AcSEC is concerned about potential unintended consequences that may result from the application of the definition of "impracticability" in paragraph 11. Although AcSEC supports the intent of paragraphs 11(b) and 11(c), it believes the wording should be clarified to reduce any unintended consequences. For example, paragraph 11(c) potentially could unduly restrict retrospective application for accounting changes that currently are required to be applied retrospectively under APB Opinion No. 20, Accounting Changes, such as changes in the method of accounting for long-term construction-type contracts. Additionally, some AcSEC members questioned whether it was the FASB's intent to require contemporaneous documentation to "objectively" determine whether information used to develop significant estimates would have been available at the time the affected transactions or events would have been recognized in the financial statements. AcSEC is concerned that the face value of paragraphs 11(b) and 11(c) could be used to avoid retrospective application for almost all situations. We believe that the Board should clarify this point.

AcSEC believes that the definition of "impracticability" should include the notion of "undue cost or effort." There may be cases in which the effects of retrospective application may not be determined without undue cost or effort. AcSEC believes that retrospective application should not be required in those cases. This notion is particularly important for entities that are reporting under U.S. generally accepted accounting principles for the first time.

Additionally, the interaction of the proposed Statement with the current auditor independence rules may result in undue cost to an entity. For example, a scenario could be envisaged in which an auditing firm ceases an audit relationship and begins providing certain "prohibited services," such as valuation or actuarial services. Providing prohibited services would preclude continuation of any audit work, including the updating of the firm's previously issued audit report on financial statements that are restated, due to independence conflicts. If an accounting policy change affects periods audited by the predecessor firm, the successor audit firm would be required to re-audit the affected transactions. Similarly, there may be issues if the predecessor auditing firm no longer exists. These examples may result in undue cost to an entity and highlight the need to consider the audit implications of a retrospective application approach.

Further, paragraph 22 appears to be inconsistent with paragraph 11. Paragraph 22 states that "...[a]n entity shall not assert that retrospective application of pre-change interim periods of the fiscal year in which the change was made is impracticable." That may not always be the case, particularly in relation to a new standard (versus a voluntary accounting policy change). Although it may be rare that an entity would assert that retrospective application is impracticable for changes made in an interim period, it is inconsistent to suggest that in all cases any entity would be able to retrospectively apply an accounting policy change occurring in an interim period.

## Other Matters

- 1. The Board should make clear that the conclusion that voluntary changes in accounting principle should be accounted for retrospectively will not lead to a presumption that new accounting standards should require retrospective application. The Board also should consider how requiring retrospective application for voluntary changes in accounting principle will affect future Securities and Exchange Commission and Emerging Issues Task Force pronouncements.
- 2. Paragraph 5, and in particular the second sentence of that paragraph, may suggest that an entity is to consider preferability when initially determining its accounting principles without regard to permitted choices available under various standards. For example, AcSEC is concerned that this guidance might preclude use of the indirect method of presentation of the statement of cash flows, which is permitted by FASB Statement No. 95, Statement of Cash Flows. The Board should clarify whether it intended to establish guidance on the initial adoption of accounting principles. In addition, some AcSEC members believe that it might be useful for the Board to develop a framework for determining the preferability of accounting principles in the future; however, AcSEC believes that such guidance is beyond the scope of the proposed Statement.

- 3. AcSEC agrees that changes in depreciation methods should be treated as changes in estimates. Some AcSEC members are concerned, however, that paragraph 17 may be providing guidance on determining the preferability of depreciation methods that does not currently exist in authoritative accounting literature, and they questioned whether such guidance would not more appropriately result from an FASB project on depreciation.
- 4. APB Opinion No. 20 requires that the pro forma effects of retroactive application of an accounting principle include both (a) the direct effects of the change and (b) nondiscretionary adjustments in items based on income before taxes or net income, such as profit sharing expense and certain royalties, that would have been recognized if the newly adopted accounting principle had been followed in prior periods. The final Statement should make clear whether retrospective application of an accounting principle does or does not include such nondiscretionary adjustments. If the Board decides that retrospective application of an accounting principle should not include such adjustments, AcSEC recommends that the Board require disclosure of the fact that such adjustments have not been made.
- 5. The final Statement should include a definition of "cumulative effect of applying a change in accounting principle." Such a definition would be useful when retrospective application is not practicable or when a new standard requires reporting of the cumulative effect of a change. The Board also should consider addressing situations in which the cumulative effect of a change in accounting principle on all affected periods cannot be determined, but the cumulative effect on a number of accounting periods can be determined.
- 6. The final Statement should include a definition of "prospective application." AcSEC recommends that a definition similar to paragraph 5 of IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors, be included in the final Statement.
- 7. Paragraphs 38 (Materiality) and 39 (Historical Summaries of Financial Information) from the original APB Opinion No. 20 provide relevant and useful guidance and should be retained in the final Statement. The final Statement also should include illustrative examples, particularly on implementing the notion of impracticability, as well as a table of concordance (similar to that in IAS 8).
- 8. The Board should clarify the disclosure requirement in paragraph 19(b)(1). Some AcSEC members read this paragraph to require disclosure of what the reported financial position and current-period results of operations would have been had the new accounting policy not been adopted. We do not believe that was the Board's intent, nor do we believe it is appropriate.

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We appreciate the opportunity to comment on the proposed Statement. Representatives of AcSEC would be pleased to discuss our comments with the Board members or staff.

Sincerely,

Mark M. Bielstein Mark M. Bielstein, Chair

Accounting Standards Executive Committee

D.J. Gannon, Chair

Short-Term International Convergence Task Force