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CFGINSIGHTS



INDUSTRY TRENDS AND DEVELOPMENTS FROM THE CORPORATE FINANCE GROUP, INC.

Welcome to the Summer edition of CFGInsights. Here, we provide you with a round-up of the most pressing accounting and reporting issues that companies face today.



SEC COMMENT LETTERS: WHAT ARE THE CURRENT HOT TOPICS?

Addressing SEC comment letters can be an arduous process. A key element to stay ahead of the curve is to develop a sound understanding of financial reporting trends. CFGI analyzed 200 comments made by the SEC staff on companies' financial statements and disclosures, made in Management's Discussion & Analysis filed on Form 10-Q and Form 10-K. What we found is that there are a handful of key accounting areas that have been focused on by the SEC:

INCOME TAXES. The SEC staff has asked registrants to disclose factors impacting the effective tax rate; earnings in countries with lower or higher statutory tax rates and their impact on the effective rate as well as the relationship between the foreign and domestic effective tax rates. Additionally, the SEC staff has asked registrants to disclose the relationship between foreign pre-tax income and the foreign effective tax rate for their foreign operations (Item 303(a)(3)(i) of Regulation S-K and Section III.B of SEC Release 33-8350).

REVERSALS OF INCOME TAX VALUATION ALLOWANCE. The SEC staff has asked registrants (especially if they have a history of losses) to present their evaluation regarding the likelihood that the registrant would generate sufficient future taxable income to realize the net deferred tax assets.

**READ MORE FOR DETAILS ON PREPARING AND AVOIDING
SEC COMMENTS >>**



PERSPECTIVES

USING QUALITATIVE IMPAIRMENT TESTING FOR INDEFINITE LIVED INTANGIBLE ASSETS.

Is there an opportunity to reduce testing and gain efficiencies in impairment testing?

ASU 2012-02 Intangibles-Goodwill and Other (Topic 350):

Testing Indefinite-Lived Intangible Assets for Impairment provides companies an opportunity to do just that. What are the requirements?

How are companies making it work to their advantage?

**READ MORE FOR FULL DETAILS
ON OBSERVATIONS >>**



COMING SOON

- FASB to issue revised lease accounting guidance: Significant accounting implications to accounting systems, processes and controls to be considered.
- Expiration of limited liability period for XBRL filings: How to ensure your company is prepared and ready to respond.

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Our team of former top-rated "Big 4" accounting professionals advises clients on complex issues including all aspects of U.S. GAAP accounting, SEC reporting, SOX compliance, business process and financial system redesign and many other areas. We provide expert consultations on technical policy matters, restatements, carve-outs, audit readiness and due diligence, in addition to filling interim accounting, reporting and tax roles. We can also augment your team by providing highly-skilled resources to review policies and procedures, SEC documents and contractual arrangements and highlight areas of focus.



SEC COMMENT LETTERS: WHAT ARE THE CURRENT HOT TOPICS? (CONTINUED)

Top Topics in SEC Comment Letters	
Omitted/Insufficient Information	27%
Operational Information	22%
Investments	13%
Equity & Share-based Compensation	8%
Revenue	6%
Valuation	6%
Commitments and Contingencies	6%
Business Combinations	6%
Income Taxes	4%
Debt	2%
Total	100%

Source: Company 10-K and 10-Q filings, CFGI.

REVENUE. Milestone arrangements, proportional performance models, contingent consideration in revenue contracts, extended payment plans with customers, warranty obligations and sales return reserves continue to be the focus of the SEC staff.

FOREIGN SUBSIDIARIES. The SEC staff has asked registrants that have foreign subsidiaries to clarify whether they can transfer funds from the foreign subsidiaries to the U.S. to assist with debt repayment, capital expenditures, and other expenses of the business, and state whether the registrant has the ability to do so, as well as to disclose the amounts that are not freely transferrable (Rule 5-02.1 of Regulation S-X). Additionally, the SEC staff has asked registrants to enhance their liquidity disclosures to quantify the amounts of foreign cash and cash equivalents at the end of the reporting period, address the potential impact on liquidity of having this cash outside the United States and state whether they would need to accrue and pay taxes if such foreign cash was repatriated. Also, the SEC staff expects that accounting policies regarding consolidation and functional currency of the subsidiaries are disclosed by registrants.

OPERATIONS IN COUNTRIES DESIGNATED BY THE US DEPARTMENT OF STATE AS STATE SPONSORS OF TERRORISM. State sponsors of terrorism (Cuba and Iran, for example) are subject to U.S. economic sanctions and asset controls. The SEC staff has asked registrants to describe the nature and extent of any past, current, or anticipated contacts with entities or operations in countries designated as state sponsors of terrorism, whether through direct or indirect arrangements.

CONTINGENCIES. The SEC staff has requested that registrants include more robust disclosure regarding legal proceedings, environmental remediation obligations and other contingencies stating whether a loss contingency is probable or reasonably possible and providing the range of possible outcomes (ASC 410-30-50 and ASC 450-20-50).

EXECUTIVE COMPENSATION PROGRAMS. The SEC staff has asked registrants to provide information regarding the total compensation pool, target and maximum values for each performance measure (including non-GAAP measures and how they are calculated, a description of each officer's individual objectives and actual results for each performance measure, etc.).

DEBT MODIFICATION. With regard to debt modifications, the SEC staff has continued to ask whether registrants have properly accounted for debt modifications (present value of the original and modified debt instrument should be compared in order to determine whether extinguishment accounting shall be applied to the original debt). The SEC staff has also asked registrants to provide additional information and enhance disclosures regarding gains and losses recorded on extinguishment of debt as well as the accounting for deferred financing costs related to the original debt.

BUSINESS COMBINATIONS. The SEC staff frequently asks registrants how they determined the acquirer in the business combination, and determined whether or not certain assets should be recognized (e.g., customer

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SEC COMMENT LETTERS: WHAT ARE THE CURRENT HOT TOPICS? *(CONTINUED)*

relationships acquired in a business combination). Also, the SEC staff expects registrants to disclose the qualitative factors for the goodwill recognized, methods and assumptions applied to value contingent consideration related to a business combination, and, in accordance with Rule 3-14 of Regulation S-X, file required financial statements for each significant acquisition (if significance tests were met).

Overall, the SEC's focus in its comments has long centered on the depth and adequacy of disclosures. Addressing these comments can be a tall order for a company. Letters often arrive at inconvenient times and responses are required within a short timeframe.

To minimize the burden and likelihood of receiving follow-up comments, consider the following strategies:

1. Pay particular attention to these SEC focus areas and ensure your company's relevant reporting and disclosures are adequate and thorough;
2. Anticipate potential SEC comments about key judgments and be ready to answer questions before they come by preparing internal documentation in a manner that can be easily converted into a formal response to a comment letter;
3. Track recent SEC releases and other resources to keep your organization abreast of the latest guidance;
4. Identify an internal plan for comment letter response, including resources that will assist when comment letters are received. ■



PERSPECTIVES: USING QUALITATIVE IMPAIRMENT TESTING FOR INDEFINITE-LIVED INTANGIBLE ASSETS *(CONTINUED)*

Accounting Standards Update 2012-02, Intangibles-Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment (ASU 2012-02), allows companies to apply a qualitative impairment test to intangibles with indefinite-lives. For many companies, this presents an opportunity to reduce the resources used on quantitative impairment tests of core intangible assets such as trademarks, trade names, or intellectual property (e.g., R&D, FCC licenses, etc.).

The revised standard allows an entity to assess qualitative factors to determine whether events and

circumstances indicate that it is more likely than not (i.e., a likelihood of more than 50%) that an indefinitely-lived intangible asset is impaired. If an entity concludes that it is NOT likely that the asset is impaired, no further action is required. An entity can choose to perform the qualitative assessment on none, some, or all of its indefinitely-lived intangible assets. In addition, an entity can bypass the qualitative assessment for any indefinitely-lived intangible assets in any period and proceed directly to the quantitative impairment test, and then choose to perform the qualitative assessment in subsequent periods. ■



TRENDS IN MATERIAL WEAKNESS DISCLOSURE

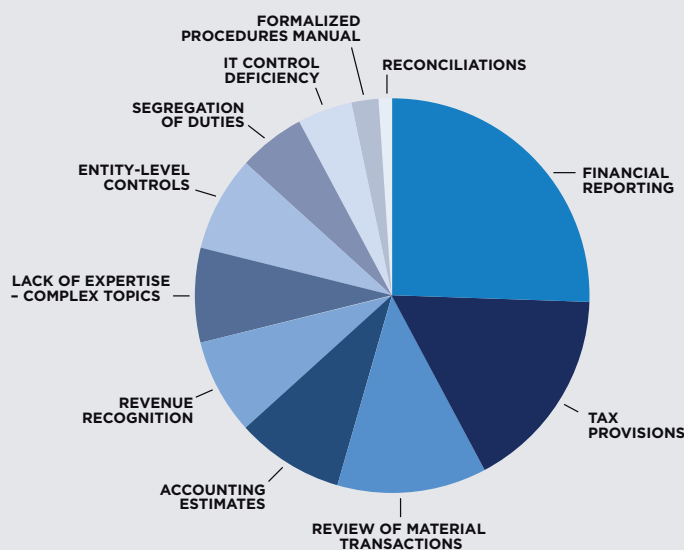
A material weakness is when a control is missing, designed improperly, or not operating effectively such that a material error could exist in the financial statements. It is the most severe classification of a control deficiency and requires disclosure in the financial statements, as well as reporting to those responsible for governance. Given the additional scrutiny on controls from an audit perspective, CFGI examined filings over the past quarter to identify trends in the types of deficiencies that companies are identifying as material weaknesses. Detailed below are three of the most prevalent issues resulting in material weaknesses:

INADEQUATE CONTROLS AROUND FINANCIAL REPORTING. Controls around the reporting of financial information are just as important as the controls to make sure financial information is recorded properly in the first place. Companies have identified material weaknesses primarily in the area of review of financial statement disclosures. Either disclosures were not prepared by employees with the requisite knowledge or companies

lacked formalized controls around reviewing the financial statement disclosures.

TAX PROVISION. Companies that reported material weaknesses struggled with the design and operation of controls covering the completeness and accuracy of the tax provision. Many companies recognized that they do not have the proper personnel in place to ensure that the process was properly controlled and misstatements would be identified. Companies found they needed more people involved in the process, as well as people with technical expertise in the area.

REVIEW OF MATERIAL TRANSACTIONS. The control environment at companies is typically designed around recurring processes and procedures. CFGI identified numerous circumstances in which companies did not have control procedures in place to handle infrequent or one-off situations. These types of transactions are such that companies are forced to react from a control design perspective rather than build out policies and procedures for handling beforehand. ■



TYPES OF MATERIAL WEAKNESSES

CFGI examined filings over the past quarter to identify trends in the types of deficiencies that companies are identifying as material weaknesses.



WHY CFGI?

At CFGI, we define our success by the quality of our work and the satisfaction of our clients. Through our deep knowledge base, industry expertise and passion for client service, we provide value add solutions to address client needs. We have built a reputation as the go-to solution for all critical finance and accounting projects and continue to build our business by attracting the industry's best professionals and supporting them with the cumulative expertise of our firm. When you partner with CFGI, you gain access to a full-service financial consulting and corporate finance team. Through our well-rounded operational and technical expertise, our team is ready to deliver the services and support needed to achieve your goals quickly, efficiently and effectively.

Whether it is assistance evaluating and documenting complex technical accounting issues, assistance with your financial close process, financial reporting and tax process, or assistance with your SOX process and documentation, we are uniquely positioned to help you with your needs. ■