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Eisner Hosts the Panel, "Is Your Company Ready to go Public?"

Eisner hosted a panel seminar on December 1, 2009, titled "Is Your Company Ready to go Public?" The event was designed to educate CEOs and CFOs about the process of going public and the steps that need to be taken to successfully undertake the initial public offering ("IPO") process. Michael Breit, head of Eisner's services to public companies group, moderated the event.

In This Issue

The panelists were:

Peter LaFlèche of Morgan Joseph & Co. Mr. LaFlèche is a managing Director and head of the firm's consumer and leisure industry group. Mr. LaFlèche has over 20 years of industry experience. Morgan Joseph & Co. Inc. is a full service investment banking firm with over 130 employees and offices in twelve cities dedicated to serving middle market companies. The firm's primary focus is on providing financial advisory and capital raising services in the U.S., Asia and Europe.

Steven Dryer of Arent Fox. Mr. Dreyer is a partner in the corporate practice at the firm. He represents various public and private companies in connection with their merger and acquisition, joint venture, capital formation and commercial contractual activities. As a member of the construction group, Mr. Dryer attends to the merger & acquisition, licensing, corporate and contractual needs of architectural and engineering clients of the firm.

Eric Altstadter of Eisner LLP. Mr. Altstadter is partner-in-charge of the firm's Long Island practice and a member of the services to public companies group. Mr. Altstadter has helped numerous clients through the complex financial reporting and compliance issues associated with the filing of registration statements with the Securities and Exchange Commission and raising capital from other sources.

Neil Goldenberg of Eisner LLP. Mr. Goldenberg leads Eisner's internal audit

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and risk management services group which specializes in independent internal audit, Sarbanes-Oxley Section 404 compliance and monitoring, information technology risk, SEC accounting and reporting advisory services, and evolving corporate governance matters. Mr. Goldenberg is also the partner-in-charge of the technology assurance and advisory services practice at Eisner.

Mr. LaFlèche began the panel with a discussion on the current IPO market conditions, which, in general, show signs of improvement with significant indicators showing a rebound since March 2009. Mr. LaFlèche pointed out that a number of IPO sectors including retail, energy and biotech are showing high percentage gains from a year ago. Indeed, it is possible that 2009's total IPO issuances will exceed 2008 because last year's 4th quarter was especially quiet for IPOs. "The IPO window is open", Mr. LaFlèche said.

Mr. Breit directed the following questions to the speakers:

What do you need to go public?

Mr. Dreyer provided four key points:

- Carefully build the skill set of senior management and the board members who are advising them
- Craft the 'story' – the bedrock message of the company that covers the products or services, the team, market size and prospects for growth
- Insist on financial statements that are complete, show a track record, and are built on and supported by sophisticated systems
- Position the company within a strong or innovative sector

When is the right time to go public?

Mr. LaFlèche answered by citing two tipping points:

- Within the company's sector, are comparable entities doing well? Simply put: is the market 'hot'?
- When there is a high confidence level in management and management controls, forecasts and projections become reasonable and actual results are close to projected results. Can the company's projected growth sustain the influx of capital?

What are the financial statement requirements?

Mr. Altstadter noted that in addition to the basic audited financial statement requirements involved with preparing for an IPO, financial managers need to pay particular attention to the age of the financial statement and the need to present unaudited stub period financial statements. He also spoke about the different requirements involved with development stage companies, entities with less than three years of operating experience and entities that were created from predecessor entities or which were formed through acquisition.

What is the importance of controls and IT processes?

Mr. Goldenberg recommended that an entity carefully review its current state of internal controls and forecast its post-IPO needs. He also spoke about right-sizing – the strategy of having the right people and skills placed against systems requirements. He then spoke about Sarbanes-Oxley Section 404, stating that the management certification of internal controls remains very much in force.

What's the role of the Board and its key committees?

Mr. Dreyer reiterated the need for the board to augment and balance the skill sets found within company management. As well, company management should expect a strong board to establish a "tone at the top" that will help direct how the company conducts its business. Critically important is having a qualified, financially literate director on the audit committee to work with the CFO as the business plan is launched. Mr. Dreyer provided details as to the requirements of outside directors serving on the three key boards: audit, compensation and nominating; as well as the values and challenges of establishing and using Advisory Boards.

From the Bar...

It's 2010: Do You Know Where Your D&O Policy Is?

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The first decade of the new millennium might be fairly characterized as the decade of high-profile corporate scandals and securities litigations. In 2001, there was Enron. In 2002, Worldcom and IPO Laddering entered the "big-case" lexicon. In 2004, Europe jumped on the bandwagon, adding Parmalat to the list of big corporate scandals. More recently, the subprime/credit crisis and the ponzi schemes orchestrated by the likes of Bernard Madoff and Allen Stanford have dominated the business press and generated numerous lawsuits and regulatory investigations. A common allegation in many of these cases is that certain directors and officers of the defendant company should be held personally liable because they either participated in the alleged fraud themselves or because they failed to act responsibly as gate keepers to protect shareholder value from corporate malfeasance.

Despite the constant reminders of high exposure securities litigation and the resultant personal exposure to directors and officers, many directors and officers still give little attention to the protections that can be provided to them through their company's Directors and Officers Liability ("D&O") insurance policies.

The ongoing financial crisis can be expected to give rise to even more such lawsuits – not to mention corporate bankruptcies and the D&O litigation often associated with those events. So it is more important than ever that directors and officers are actively engaged in the discussions and decisions about structuring their company's D&O insurance programs to ensure that the D&O coverage protects both the financial needs of their companies and their personal financial interests -- especially in the event the company cannot honor its indemnification obligations to them. Discussed below are some key issues that companies and their directors and officers should keep in mind when purchasing D&O coverage.

What Type of D&O Coverage Should We Buy?

D&O coverage is intended to work, in the first instance, in tandem with corporate indemnification provisions, which are generally contained in a company's by-laws, articles of incorporation, indemnification agreements, or officer employment agreements. All fifty states, by statute, allow corporations to provide indemnification of directors and officers by the corporations they serve. As a general proposition, the corporate entity indemnifies its directors and officers for legal expenses, judgments and settlements these individuals incur in actions and investigations pending against the individuals arising from lawful corporate capacity.

Given that D&O coverage is intended to conform to a corporation's indemnification obligations to its directors and officers, D&O policies typically contain at least two coverage parts, commonly known as "Side A" and "Side B." Side A coverage protects the personal assets of the insured directors and officers by providing direct insurance of individual directors and officers when the corporation does not or cannot provide indemnification to its directors and officers. The two most commonly-cited examples of Side A D&O claims are shareholder derivative actions brought against directors and officers suing on behalf of the corporate principal and bankruptcy-related D&O litigation. In the case of shareholder derivative litigation, many states prohibit the corporation from indemnifying its directors and officers for settlements or judgments in such claim because indemnification in such a situation would have a circular result: The corporation would be indemnifying its directors and officers for a settlement or judgment they owe to the corporation itself. In the case of bankruptcy-related D&O litigation, the applicability of indemnification is not the key issue: the issue in these cases is that because the corporate principal is insolvent, it has no funds with which to provide the required indemnification to its directors and officers.

But what about the other ways in which a D&O policy can respond to a claim? Side B coverage provides the company with what is effectively balance sheet protection by reimbursing the corporation when it is required or permitted to indemnify its directors and officers. Some D&O policies also contain "Side C" coverage for loss incurred by the company itself. In the case of publicly-traded companies, the "Side C" coverage typically is limited to claims against the company arising under federal or state securities statutes or under SEC rules and regulations.Traditional public company D&O policies contain Side A, B, and C coverage with a single aggregate limit of liability, meaning that the policy limit of liability can be reduced -- or depleted -- through payments of loss under any coverage part. For example, if the full limit of liability is used to defend the company in a securities class action, there would be no remaining limits of liability available for directors or officers who might subsequently be named as defendants in another D&O claim.

To respond to this concern, a number of D&O insurers now offer "Side A only" or "Side A DIC" (i.e., Difference-in-Conditions) D&O policies, with a dedicated limit of liability covering directors and officers when indemnification and standard D&O insurance (i.e., the underlying Side ABC policy with one aggregate limit of liability) may be unavailable to them. As discussed above, the two primary sources of non-indemnifiable Side-A exposures that directors and officers of publicly-traded companies face arise in connection with shareholder derivative actions, and the financial inability of the company to fund its indemnification obligations.

Although "Side A only" and "Side A DIC" D&O policies have been available for a number of years, insureds and insurance brokers historically questioned the need for such policies, particularly given the plentiful and relatively inexpensive coverage limits that could be purchased in a traditional D&O insurance program format providing all three (i.e., Sides A, B and C) coverages. Recent events, including the stock option backdating scandal, the subprime/credit crisis and various ponzi schemes, have caused directors and officers to sit up and take notice of the significant exposure they could personally face if their corporate principal is unable to indemnify them for a lawsuit or investigation if corporate indemnification and underlying D&O insurance proceeds are unavailable to them.

How Much D&O Coverage Should We Buy?

Public company insureds are often advised by their insurance brokers to purchase limits of liability that are, at a minimum, ten percent of the company's market capitalization. This general rule of thumb is subject to many variables, including the type of business the company engages in; the markets the company operates in; fluctuations in the company's stock price; and inside stock ownership.

Another key consideration here is the business goal of the D&O program. If the goal of the D&O program is to provide the company with balance sheet protection, the company may want to maximize the limit of liability on a traditional D&O program that contains one aggregate limit of liability for Side A, B and C claims. However, if the goal of the D&O program is to protect the personal assets of the directors and officers and provide "sleep insurance" to these individuals, the company may want to purchase additional "Side A only" or "Side A DIC" limits of liability.

In a perfect world, the D&O insurance program's total limit of liability would fully respond to both the costs of defense and any settlement or judgment for the most high exposure lawsuits that publicly-traded companies and their directors and officers face: the class action lawsuits brought under the Securities Act of 1933 or the Securities Exchange Act of 1934 (as well as those SEC rules and regulations promulgated in connection with these statutes). If a securities class action survives past the motion to dismiss stage, the electronic discovery costs alone could run in the millions of dollars. With respect to regulatory investigations and proceedings, discovery costs can run in the millions of dollars, even at the very early stages.

Moreover, if the directors and officers each have to engage separate counsel because of potential conflicts of interest, the costs of defense can escalate quickly and exponentially. Even after spending millions of dollars on defense costs, the company and its directors and officers may be faced with an enormous settlement demand or potential judgment. According to a Carpenter Moore (an executive liability risk management services provider) survey of securities class action settlements from 2004 through the first quarter of 2009, the average securities class action settlement was $47.3 million.

Understand the Policy

There is no one-size-fits-all D&O policy. The terms and conditions of a D&O policy, unlike some other types of insurance, are often heavily negotiated. Some of the most common definitions in D&O policies, such as "Insured" or "Claim," contain subtle differences that may lead to drastically different coverage results. For example, if a non-director or officer of a company is named as a defendant in a lawsuit, the coverage outcome could hinge on whether the definition of an "Insured" includes "all employees" or just "current and former directors and officers."

As another example, if a governmental or regulatory agency, such as the SEC, initiates an investigation of the company and the company's directors and officers, the coverage outcome could hinge on whether the definition of "Claim" is triggered by "a formal investigative order" or by a "Wells" notice. The "Wells" notice is the last stage of the SEC's investigation before the SEC's Division of Enforcement decides to bring an enforcement proceeding. During the time period between the when the SEC issues a formal order of investigation and its "Wells" notice, insureds can spend millions of dollars in defense costs in responding to the SEC's broad document requests.

Companies should consult with their insurance brokers and outside counsel to assess whether the proposed terms and conditions of the D&O policy meets their coverage needs. With the increased competition in the D&O marketplace, D&O insurers are often willing to modify and enhance certain terms and conditions of their policy forms.

From the Bar… is designed to present our readers with the views of counsel from outside Eisner LLP. Please visit www.eapdlaw.com for more information on Edwards Angell Palmer & Dodge LLP.

Pension funds and other investors have asked the SEC to consider requiring companies to disclose climate-related risks in their quarterly and annual filings. "This is calling for real transparency on material risks that have a profound impact on share value of companies," said Mindy Lubber, president of Ceres, a group of investors and environmentalists that have been involved in this matter. "These are now real on-balance sheet risks. They are material. They ought to be disclosed." The group also wants the SEC to mandate that emissions data and associated risks, opportunities and management strategies are analyzed by companies and disclosed. Two years ago, this group sent a similar request to the SEC but say their requests did not receive much consideration under the George W. Bush administration.

Textron Loses Work Product Case

The ongoing Textron Inc. ("Textron") litigation recently provided a significant ruling pertaining to work product doctrine in the context of documents created by in-house accountants and counsel. On August 13, 2009, the First Circuit issued a 3-2 en banc decision that rejected Textron Inc.'s position that its internal tax accrual workpapers were protected by the work product doctrine. The decision is a victory for the Internal Revenue Service ("IRS") in its longstanding effort to gain access to these workpapers and a major blow to companies that utilize the privilege. Despite their creation by in-house accountants under the direction of counsel and by counsel themselves; the First Circuit deemed these workpaper documents that were created in the ordinary course of business and not for litigation purposes.

History

The procedural history can be summarized rather briefly. As stated above, the workpapers central to this matter were originally created by Textron in-house counsel or by Textron in-house accountants under the guidance of their in-house counsel. These workpapers listed certain positions on Textron's 2001 tax returns and were coupled with an analysis of litigation risks associated with each position. Specifically, the litigation risk analyses entailed the probability of litigation and reserves associated with each position. As part of an audit, the IRS requested these papers in 2005 and Textron refused to supply these documents on the grounds that the documents were protected under the attorney-client privilege.

The IRS and Textron initially squared off in district court and, in 2007, the district court held that these documents were created to gauge the adequacy of reserves in case of litigation and therefore, were protected work product. The crucial factor for the district court was that the workpapers were created in contemplation of litigation. The court did not subscribe to the IRS's position that these documents were created in the ordinary course of business. Furthermore, the district court did not agree that the attorney-client privilege was effectively waived because Textron disclosed the documents to a third-party, their outside auditors, Ernst & Young, LLP.

The matter journeyed through the courts and encountered appeals and remands and ultimately led to the First Circuit's recent decision. The First Circuit's decision is based on the premise that the workpapers were not created in anticipation of litigation. According to the majority, these workpapers would likely have been created absent any potential of litigation and were created for both litigation and non-litigation purposes. The Court focused on evidence that indicated that these workpapers were created to meet GAAP requirements and appeared to place less emphasis on evidence indicating that the workpapers were created for potential litigation.

The Work Product Doctrine

The Federal Rules of Civil Procedure apply to documents "prepared in anticipation of litigation or for trial." While documents clearly prepared for litigation receive the protection, those documents that are not clearly trial materials have divided the courts. The majority of courts hold that the documents must be created because of prospective litigation and the minority holds that the primary motivating purpose of document creation must be to assist in pending or impending litigation. In essence, the majority view casts a wider net of protection over documents. While not exact, the Textron court resembles the minority view by only protecting documents prepared for pending or impending litigation. The Textron majority focused on the fact that the documents were not prepared for pending or impending litigation. To support its position, the Textron majority appeared to rely on the assumption that trial lawyers would not view these workpapers as case preparation materials.

Eisner Analysis

The decision by the First Circuit sets a difficult precedent for many companies such as Textron. While the government and the IRS must collect revenue, it should not be at the expense of the work product doctrine. The implication of the First Circuit's ruling is certainly problematic and predictably far-reaching. One exception to the work product doctrine may lay the groundwork for more exceptions. The First Circuit's exception coupled with any future exceptions may significantly damage the protection currently afforded by the doctrine and may ultimately render it useless for certain taxpayers. At minimum, companies that now create dual-purpose tax/accounting documents should be cognizant that the attorney-client privilege may not automatically exist. More importantly, companies should note that tax and accounting documents that were partially created in anticipation of potential litigation may ultimately result in handing over their strategies to the IRS.

Whither IFRS?

Slightly over a year ago, the SEC released its roadmap for the use of International Financial Reporting Standards (IFRS) by domestic reporting entities in the United States. The proposed roadmap included the voluntary use of IFRS by the largest users by industry beginning in 2010.

The minor matter of a "financial crisis" in the U.S., and worldwide, caused the SEC to first push back the comment deadline, then to seemingly abandon the concept altogether as such a change was viewed as a low priority by the new administration led by SEC Chairperson Mary Schapiro. Additionally, the elasticity displayed by the International Accounting Standards Board (IASB) in the face of pressure from the European Union indicated to U.S. users that, perhaps, IFRS was not ready for primacy. As a result, efforts by preparers and auditors to get up to speed on the principles of IFRS seemed, for a time, to be a waste of time and resources in a fragile economy.

Now that the worst of the crisis has apparently passed, post-mortems on the responses of the IASB and the U.S. Financial Accounting Standards Board (FASB), as well as their continuing standard-setting agendas are starting to again bring cries of "can't everybody just get along?" The need for one set of high quality global accounting standards is clearly evident. The chairman of the FASB, Robert Herz, has often and consistently acknowledged this. Nearly as often, whether out of modesty or practicality for its acceptance, he has also acknowledged that the FASB is not that standard setter. It is, however, fairly well accepted that as voluminous and "rules-based" as U.S. Generally Accepted Accounting Principles (GAAP) are, they are still the most comprehensive rules available, covering many areas that IFRS do not. So, is IFRS the answer?

The chairman of the IASB, Sir David Tweedie, has called for the SEC to move forward with its proposal to allow or require IFRS by domestic registrants. There have been several reports, both within and outside the IASB, that the convergence efforts with the FASB be suspended in order for the IASB to save money and time by concentrating its efforts on improving IFRS for its users, irregardless of any remaining differences with U.S. GAAP. It is understandable that the IASB wants the SEC to commit, which would provide the IASB with the impetus to continue the convergence efforts and open up potential funding opportunities. By the same token, if the SEC does not make such a commitment, then the IASB has little incentive to continue the convergence efforts. It would then better serve its constituency by focusing its efforts on priorities set by their users, and not some of the farther-reaching measures being addressed under convergence.

So, where does the SEC stand? The SEC's new chief accountant, James Kroeker, and commissioner Elisse Walter recently remarked that the IFRS roadmap was not abandoned and that the SEC was making its way through the many comment letters it had received. Although not committing to what kind of time table would be in the new release, a likely casualty of the delay would be the 2010 initial filing date for voluntary reporting if the SEC decides to keep that part of the roadmap. It is important to remember that the roadmap or whatever it may be called upon its next iteration, once adopted, is not a change in regulation, but only a list of steps that the SEC will consider in the coming years as it addresses the issue of reporting under IFRS for domestic registrants. Failure of specific points of the release, or rousing successes, will not spell doom or acceptance, but the analysis of the steps in their totality will be used to judge the ultimate acceptance of IFRS or the decision to stick with FASB's U.S. GAAP.

The continuing efforts by the IASB to improve their standards, not only as brought to light by the financial crisis, but also into areas that IFRS do not currently address, as well as the convergence efforts, whether they be called convergence or co-improvement projects with the FASB, are critical to the acceptance of IFRS by preparers, users, auditors, regulators and analysts in the U.S. and around the world. Based on the projects on the FASB's and IASB's agendas, and their recent announcement of "redoubling" their efforts, including the scheduling of monthly joint meetings, future U.S. GAAP will have some very striking similarities to IFRS and vice versa. Whether or not IFRS is ultimately adopted as required or optional by the SEC, the U.S. GAAP used by registrants will, in many respects, be IFRS-like.

The continued convergence or improvement projects on both the FASB's and IASB's agendas were also an important milestone in the proposed roadmap. As envisioned, the end result of these efforts will bring users of IFRS and U.S. GAAP to a level of equivalency, the differences of which will only matter to the most meticulous of bean-counters. The two boards have targeted June 2011 as the completion date for the projects. If successful, these changes will make a move by the SEC to accept IFRS important only in the seeming ceding of standard-setting to an entity outside their control. It is critically important to all users of financial statements that they keep an eye on these developments, and the money and resources expended will be well spent.

Selected Provisions of the Proposed Roadmap (SEC Release 33-8982)

- Milestones to be evaluated in 2011 include:
  - Improvements in accounting standards
  - Improvements in XBRL for IFRS
  - Education and training
  - Evaluation of early-adopters

- Early adoption election for U.S. companies among the 20 largest companies in "IFRS industries" (estimated to be ~110 companies) for FYE after 12/14/2009

- Mandatory adoption of IFRS for FYE after 12/14/2014 for large accelerated filers, 2015 for accelerated filers and 2016 for non-accelerated filers (including smaller reporting companies)

In his address to the AICPA National Conference on SEC Developments, SEC chief accountant James L. Kroeker said that independent auditors should consider the interests of the investing public — not just their audit clients — when conducting audits. "I believe that the accounting profession has made great strides restoring investor confidence and the perception of what it means to be a Certified Public Accountant," said Mr. Kroeker. "I believe that the vast majority of accountants are honest hard-working professionals who simply want to 'do the right thing.'"

Revisions to FASB Guidance on Measuring Liabilities at Fair Value

Why the Update & When is it Effective?

According to Topic 820--Fair Value Measurements and Disclosures, fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." The fair value measurement assumes that a liability is exchanged in an orderly transactionbetween market participants and that the risk of nonperformance does not change as a result of the exchange. Entities have expressed concern that there may be a lack of observable market information (e.g., quoted price for identical liability in an active market) to measure the fair value of a liability, often because of contractual or other legal restrictions on the liability being valued. Therefore, some entities have questioned how to measure the fair value of a liability in a hypothetical transaction when a restriction prevents such a transfer. Considering that some liabilities (e.g., bonds) are traded in the marketplace as assets, questions have been raised about whether prices of debt instruments traded as assets represent the fair value of that instrument for the issuer (obligor). Considering these issues, the FASB has issued updated guidance (Accounting Standards Update 2009-05) on the fair value measurement of liabilities in order to address these issues.

Summary of Revisions

The update to Topic 820 (Measuring Liabilities at Fair Value) indicates that when a quoted price for an identical liability is not available, a reporting unit shall measure fair value using a valuation technique that uses either (1) the quoted price of the identical liability when traded as an asset or (2) the quoted prices for similar liabilities traded as a liability or asset or a valuation technique consistent with the principles of Topic 820. Such techniques could include an income approach or a market approach. The revision also allows for certain adjustments to the quoted price of a liability traded as an asset or valuation technique used to value the liability; however, the guidance advises that adjustments (e.g., discounts) should not be made to the quoted price or the valuation technique for restrictions that prevent the transfer of the underlying liability since the affect of the restriction is implicitly or explicitly already included in the other inputs to the fair value measurement.

The amendments to Topic 820 are summarized below:

Measurement

In circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity shall measure fair value using one or more of the following techniques:

- Quoted price of an identical liability when traded as an asset or quoted prices for similar liabilities traded as a liability or asset. A reporting entity needs to determine whether the quoted price in an active market should be adjusted for factors specific to the liability and the asset. Any adjustment to the quoted price should render the fair value measurement of the liability a lower level measurement in the fair value hierarchy.

- Another valuation technique that is consistent with the principles of Topic 820. For example, an income approach using a present value technique or a market approach reflecting the amount an entity would pay to transfer the identical liability or would receive to enter into the identical liability. When applying a valuation technique, inputs shall reflect the assumptions that market participants would use in the principal or most advantageous market for the liability with the same contractual terms.

A reporting entity shall apply all applicable guidance in Topic 820 in determining fair value when the volume and level of activity for an asset or liability have significantly decreased and for transactions that are not orderly. That is, further analysis of the transactions or quoted prices is needed, and a significant adjustment to the transactions or quoted prices may be necessary to estimate fair value. Alternatively, a change in valuation technique or the use of multiple valuation techniques may be appropriate (e.g., use of both a market approach and a present value technique).

Adjustments Allowed in Measuring Fair Value

When measuring the fair value of a liability using the quoted price of the liability when traded as an asset or using a valuation technique to value the liability, the reporting entity should not adjust the quoted price of the asset or adjust inputs to the valuation technique model for the effect of a restriction preventing the liability's sale. The effect of a restriction that prevents the transfer of a liability is assumed to be either implicitly or explicitly already included in the other inputs to the fair value measurement. However, the quoted price of the liability when traded as an asset shall be adjusted for the factors specific to the asset that are not applicable to the fair value measurement of the liability. For example, the quoted price for the asset includes the effect of a third-party credit enhancement or the inclusion of a restriction preventing the sale of the asset (not the underlying liability). Also, as discussed above, adjustments are allowed when the volume and level of activity for an asset have significantly decreased and for transactions that are not orderly.

Effective Date

The new guidance is effective for the first reporting period (including interim periods) beginning after the date of issuance of the update which is August 26, 2009. A change in a valuation technique or its application resulting from the new guidance must be accounted for as a change in estimate. In the period of adoption, a reporting entity must disclose any resulting change in valuation technique and related inputs and quantify the total effect, if practicable.

According to panelists at the 2009 XBRL National Conference, registrants need to take time to document the reasons items are tagged the way they are tagged. In addition, sufficient time should be allocated to review the information even if this process is outsourced to a third party. Large U.S. public companies and foreign private issuers listed with the SEC with fiscal periods ending on or after June 15, 2009 have started mandatory filing. To date, almost 500 companies have filed financial reports in XBRL and some common errors emerged in preliminary submissions. XBRL US plans to release a set of approximately 3,000 "checks" that public companies can use to identify common errors that occur in XBRL-formatted financial statements. Many of the companies that have filed using XBRL have outsourced the work on the first and second round of filings.

The SEC will require registrants to provide written disclosure of their pay practices for all employees starting next year. They will also need to disclose why they chose a specific leadership structure and the qualifications of the board of directors, including their diversity and how that is considered when nominating director candidates. Registrants will also provide information on fees given to compensation consultants. "Through these rules, investors will better understand whether a company's compensation policies and practices are reasonably likely to increase the company's risk exposure," said SEC chair Mary Schapiro. The new rules are intended to give investors a better understanding of the stock and option awards granted to executives and directors and the background and qualifications of each director and board nominee.

New Rules on Revenue Recognition

The next time you buy a smart phone or PDA, your $200 may appear much sooner in the seller's revenue and give them a stronger boost in their current period earnings.

Scope Clarification for Software Revenue

An accounting rule change, Accounting Standards Update (ASU) 2009-14, Certain Revenue Arrangements that Include Software Elements (previously exposed as EITF Issue No. 09-3), issued by the Financial Accounting Standards Board (FASB) on October 7, 2009, will likely allow companies to recognize revenues sooner on products that bundle hardware, software and services. With the technological advances which have been made in recent years, the rules on software revenue recognition (Accounting Standards Codification (ASC) Topic 985, Software, incorporating previous guidance under SOP No. 97-2) were capturing many products that were not traditional software products, such as smart phones and other software-enabled devices. This often resulted in a deferral of revenue recognition for these products, despite the upfront cash receipts by the company and the receipt of the device and included software by the customer. The inconsistency between accounting rules and the economics of the arrangement has frustrated technology companies for years.

ASU 2009-14 modifies ASC Topic 985 by excluding from its scope (1) non-software components of tangible products and (2) any tangible products containing software components and non-software components that function together to deliver the product's essential functionality from software revenue recognition rules. Thus, companies will be able to unbundle and recognize the revenue separately for the software and non-software components (see the following discussion on ASU 2009-13.) The guidance also provides a list of factors that a vendor should consider in determining whether a tangible product is delivered with software components and non-software components that function together to deliver the tangible product's essential functionality.

Arrangements with Multiple Deliverables

A related significant change in revenue recognition will affect companies that provide multiple products or services ("deliverables") to their customers in a single arrangement. The FASB issued new guidance in ASU 2009-13, Multiple-Deliverable Revenue Arrangements (previously exposed as EITF Issue No. 08-1), that will allow companies to allocate consideration in multiple-deliverable arrangements by allowing the use of a "best estimate of selling price" in addition to third-party evidence (TPE) (previously referred to as vendor-specific objective evidence VSOE or vendor objective evidence VOE). Because companies will now be required to identify all the deliverables in an arrangement and all deliverables will be separate units of accounting, the residual method of allocating consideration for multiple-deliverable arrangements is no longer permitted under ASU 2009-13.

The challenge is certainly more than just learning the new acronyms. Companies will need to embrace system and process changes when developing, documenting, and supporting management's best estimate of selling price. The new guidance also includes new and significant ongoing disclosure requirements. Companies with multiple-deliverable arrangements are required to provide both qualitative and quantitative information necessary for a user of the financial statements to understand the revenue arrangements, the significant judgments made, and changes in those judgments that may significantly affect the timing or amount of revenue recognition.

Effective Date and Transition

The above new accounting rules are effective prospectively for arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Specific transition disclosures for multiple-deliverable revenue arrangements are required in the initial year of adoption. Companies that elect to apply the software revenue recognition guidance prospectively should also provide the transition disclosures required by the new guidance on multiple-deliverables.

Early adoption is permitted. If a company elects early application in an interim period other than the beginning of its fiscal year, it should apply the guidance on multiple-deliverables retrospectively for all prior reporting periods of that fiscal year. However, if applicable, the guidance on software revenue recognition must be adopted in the same period that the guidance on multiple-deliverables is adopted.

Alternatively, companies may elect to apply the new guidance retrospectively pursuant to ASC Topic 250, Accounting Changes and Error Corrections (previously known as FASB Statement No. 154,) and provide the applicable disclosures required by ASC Topic 250.

Latest Comments from the Commission

"Latest Comments from the Commission" intends to highlight some of the more frequently appearing quotes from recent SEC comment letters. For a complete listing of SEC comment letters and registrants' responses, please visit the commission's website at www.sec.gov.

Impairment of Long-lived Assets

You disclose that your impairment evaluation of long-lived assets, including finite-lived intangible assets, involves comparing estimates of future cash flows to the carrying amount of the asset being evaluated. Estimates of future cash flows are normally inherently uncertain. In light of the significance of finite-lived intangible assets to your reported assets, in future filings please disclose how you estimate future cash flows for impairment testing purposes, including how you attribute cash flows to specific assets being evaluated for potential impairment. Please also describe uncertainties associated with those cash flow estimates and describe the potential for reasonably possible variability. Refer to Release No. 33-8350: "Interpretation: Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations."

As a related matter, in future filings please also disclose how you determine fair value when estimated undiscounted future cash flows are less than the carrying amount of a long-lived asset being evaluated for impairment. Also address the uncertainties and subjectivity of those estimates, as appropriate.

Contractual Obligations and Uncertain Tax Positions

Financial statement footnote 15 discloses that the obligation for uncertain tax positions is $10.4 million as of December 31, 2008. In future filings please clarify whether FIN 48 obligations are included in the table of contractual obligations. If FIN 48 obligations are not included, please disclose in the narrative to the table with explanation of the basis for exclusion.

Non-GAAP Measures in Earnings Releases

We note that you present non-GAAP financial measures and related reconciliations in the form of Condensed Consolidated Statements of Income for the three and six months ended June 30, 2009 and 2008. The format presents numerous non-GAAP balances and subtotals most of which have not been individually described to investors in your earnings release. Inclusion of a non-GAAP statement of operations leaves an impression that the non-GAAP presentation represents a comprehensive basis of accounting and gives undue prominence to the non-GAAP financial information. In future earnings releases please delete the non-GAAP statements of income. If you elect to present non-GAAP financial measures, please provide the reconciliation and narrative disclosures set forth in Item 10(e)(1)(i)(C) and (D) for each individual non-GAAP financial measure presented. Refer to also to Instruction 2 of Item 2.02 of Form 8-K.

As a related matter, it appears that the various non-GAAP financial measures eliminate recurring expenses, such as financing charges, asset write-downs, foreign exchange gains or losses, litigation expenses, stock-based compensation and amortization of intangible assets, among others. Accordingly, please tell us how your presentation considers the disclosure guidance from Question 8 of the Frequently Asked Questions Regarding the Use of Non-GAAP Financial Measures. Appropriately expand future earnings releases.

Executive Compensation

We note from your disclosure under "Base Salaries" that you have incorporated by reference from your proxy statement that you target total cash compensation for your named executive officers at the 50th percentile of your peer companies. Given that you target the cash elements of your compensation packages, please briefly discuss in your applicable future filings how each element of cash compensation you provide to the named executive officers relates to the data you have analyzed from the peer companies and include an analysis of where actual payments under each element of cash compensation actually fell within the targeted range. If any of your named executive officers are compensated at levels that are materially different from the targeted levels of compensation, please also provide discussion and analysis as to why. We note from your disclosure under "Annual Cash Incentives" that you do not disclose the amount of the targets or goals in order for your named executive officers to receive their non-equity incentive plan compensation. In future filings, please provide such disclosure as applicable. To the extent you believe that disclosure of such information, on a historical basis, would result in competitive harm such that the information could be excluded under Instruction 4 to Item 402(b) of Regulation S-K, please provide us with a detailed explanation supporting your conclusion. To the extent that it is appropriate to omit specific targets or goals, you are required to provide appropriate disclosure pursuant to Instruction 4 to Item 402(b) of Regulation S-K. Refer also to Question 118.04 of the Regulation S-K Compliance and Disclosure Interpretations available on our website at http://www.sec.gov/divisions/corpfin/guidance/regs-kinterp.htm. In discussing how difficult or likely it will be to achieve the targets or goals, you should provide as much detail as necessary without disclosing information that poses a reasonable risk of competitive harm.

We refer to your disclosure under the caption "Long-Tem, Equity-Based Incentive Awards" in the proxy statement that you have incorporated by reference into your Form 10-K. We note minimal, if any, discussion and analysis as to how the annual stock option grants and performance share awards were determined. In your future filings, as applicable, please include substantive analysis and insight into how your Compensation Committee made it stock option grant and performance share award determinations with respect to each named executive officer. Refer to subparagraphs (b)(l)(iii) and (v) of Item 402 of Regulation S-K. For example, please discuss and analyze how the Compensation Committee determined the actual number of shares underlying the stock options that were awarded to your named executive officers and how and why those awards varied among the named executive officers.

Standards Update

Codification of FAS 166 and FAS 167 (ASU 2009-16 and ASU 2009-17)
The FASB issued ASU No. 2009-16, Transfer and Servicing (Topic 860) – Accounting for Transfers of Financial Assets, and ASU No. 2009-17, Consolidation (Topic 810) – Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities, on December 23, 2009. As a result, FASB Statement No. 166, Accounting for Transfers of Financial Assets, and FASB Statement No. 167, Amendments to FASB Interpretation No. 46(R), have now been incorporated into the standard-setter's Accounting Standards Codification for U.S. GAAP.

Both ASUs are effective for annual periods beginning after November 15, 2009 (i.e., January 1, 2010 for calendar year-end companies). The FASB also issued a proposed update to the application of FAS 167 (ASU 2009-17) for certain investment funds until the joint consolidation project is completed by IASB and FASB in late 2010. Examples of entities that may meet the Board's deferral criteria include, but are not limited to, mutual funds, hedge funds, private equity funds and venture capital funds. Examples of entities that do not meet these criteria include, but are not limited to, securitization entities, asset-backed financing entities, or entities formerly classified as qualifying special purpose entities. The comment period ended on January 6, 2010, and the Board has begun its redeliberations on this topic.

Proposed Exposure Draft on Subsequent Event Procedures
During the last week of 2009, the FASB exposed a proposed ASU that addresses certain implementation issues related to the requirement to perform and disclose subsequent events in accordance with FASB Statement No. 165 (codified as ASC Topic 855, Subsequent Events). The proposal would amend the guidance as follows: (1) An entity that files financial statements with, or furnishes them to, the SEC would not be required to disclose the date through which subsequent-events procedures have been performed and (2) clarify the disclosure required for reissued financial statements. In addition, the proposed ASU would clarify that non-SEC filers or furnishers must disclose the date through which these updated procedures have been performed.

Comments on the proposed ASU are due by January 28, 2010. The final ASU would be effective immediately upon issuance.

New ASUs in the New Year
The FASB issued the following Accounting Standards Updates (ASUs) in January 2010.

ASU 2010-01, Equity (ASC 505) – Accounting for Distributions to Shareholders with Components of Stock and Cash (a consensus of the FASB Emerging Issues Task Force) — This ASU incorporates the final consensus reached on EITF Issue 09-E, Accounting for Distributions to Shareholders with Components of Stock and Cash, into the Codification. The guidance is effective for interim and annual periods ending on or after December 15, 2009.

ASU 2010-02, Consolidation (ASC 810) – Accounting and Reporting for Decreases in Ownership of a Subsidiary—a Scope Clarification — This ASU addresses implementation issues related to the changes-in-ownership provisions in the ASC 810-10. It updates the scope of the decrease-in-ownership guidance to specifically include nonprofit activities and specifically exclude in-substance real estate and conveyances of oil and gas mineral rights. It also clarifies that the guidance applies to a decrease in ownership of a subsidiary or a group of assets that is a business. In addition, expanded disclosures are required related to valuation techniques used and the extent of any continuing involvement or related party interaction.

An entity is required to follow the amended guidance beginning in the period that it first adopts FAS 160, Noncontrolling Interests in Consolidated Financial Statements (now included in ASC 810-10). For those entities that have already adopted FAS 160, the amendments are effective at the beginning of the first interim or annual reporting period ending on or after December 15, 2009, and the amendments should be applied retrospectively to the first period that an entity adopted FAS 160.

ASU 2010-03, Extractive Activities – Oil and Gas (ASC 932) – Oil and Gas Reserve Estimation and Disclosures — This ASU amends the Codification to align the oil and gas reserve estimation and disclosure requirements in ASC 932 with the SEC's final rule, Modernization of the Oil and Gas Reporting Requirements. The amendments are effective for annual reporting periods ending on or after December 31, 2009.

On the Horizon:
Disclosures of Fair Value Measures

We've previously discussed that the FASB has proposed certain disclosures about fair value measurements in an exposure draft of an ASU. The previous proposal includes three new disclosure requirements:

(1) a sensitivity disclosure for fair value measurements using significant unobservable inputs (level 3), if changing one or more of those inputs to reasonably possible alternative inputs would increase or decrease the fair value measurement significantly;

2) the amounts of significant transfers in and/or out of Level 1 and Level 2 fair value measurements and the reasons for the transfers; and

(3) a reconciliation of the activities in Level 3 fair value measurements on a gross basis.

The comment period for the proposal ended on October 12, 2009. The FASB decided to defer the consideration of the Level 3 sensitivity disclosures but proceed with all of the remaining requirements substantially as described in the proposed ASU. The final update will amend Topic 820-10 and will be effective for annual or interim reporting periods beginning after December 15, 2009, except for the requirement to provide the Level 3 activity for purchases, sales, issuances, and settlements on a gross basis. The Board expects to issue a final update shortly.*

**Just before the publication date of this Alert, the FASB issued ASU 2010-06 that finalizes the new disclosure requirements for fair value measures. The final disclosures are similar to those in the proposed ASU described above and do not require entities to provide sensitivity disclosures.*

The PCAOB has re-proposed seven auditing standards and amendments that effect auditors' assessment of audit risks. These standards had been proposed in October 2008, but have been revised based on the comments received. These standards would establish requirements for procedures in an audit from the planning through the release of the auditor's report. The goal of these standards is to enhance the effectiveness of an auditor's assessment of, and response to, risk. They emphasize the auditor's responsibility to consider the risk of fraud throughout an audit and include new requirements which will improve the auditor's evaluation of disclosures. "A sound and sophisticated risk assessment is essential to performing an audit that affords investors reasonable assurance that financial statements are free of material error," said acting PCAOB chairman Daniel L. Goelzer. "These seven standards – once finalized – will serve as the bedrock for much of the board's future standard-setting".

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