

COMPLIANCE WEEK

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FIN 48 Non-compliance; Audit Reform; More

By Tammy Whitehouse — July 29, 2008

More than one quarter of large public companies are not meeting the disclosure requirements for tax reserves required under the controversial, tell-all accounting rule Financial Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*.

The consulting firm Seigel & Associates conducted a review of annual reports in the first quarter of 2008, studying the filings of 600 companies with revenues of more than \$2 billion. The firm said 28 percent of the reports it reviewed did not fully meet the disclosure mandates of FIN 48.

FIN 48 requires companies to detail where they may have uncertainties in the tax positions they've taken on corporate tax returns. Seigel & Associates published its findings in a report titled "*The Seigel Tax Reserve Report*," which firm President Brad McGee says will now be published quarterly.

In its analysis, Seigel found that companies struggled most with the "12-month look-forward rule," where companies are required to provide disclosure around tax positions that have a reasonable possibility of significant variation over the next 12 months. One in every eight companies provided no disclosure of any kind, McGee says. "There is room for improvement," he says.



McGee

McGee acknowledges that companies walked a tightrope in the first annual filing under FIN 48: providing enough disclosure to meet regulatory requirements, but not so much to give away proprietary information or details that would compromise a pending tax dispute. (Companies dislike FIN 48 chiefly because they fear it will give tax authorities a roadmap for investigations.)

"Companies that have deficiencies walk a fine line between disclosures being deficient and being overly generous with information," he says. "Clearly there enough companies that did a good job with the disclosure that it leads me to believe all companies could do it. How could one in four not comply fully with the rules? It's a little bothersome."

The Seigel report found that 280 companies in its analysis increased their tax reserves—the amount set aside pending adjustments to tax liabilities—by a total of \$8.1 billion, while 151 companies decreased their reserves by a total of \$6.8 billion, creating a net increase of \$1.4 billion.

The firm established an index for scoring companies on their FIN 48 compliance, weighing how well companies complied with six key requirements of FIN 48, including the 12-month look-forward disclosure, the tabular presentation, and other requirements.

Based on that scoring system, a score of 100 would denote satisfactory compliance with FIN 48. The aggregate score for companies covered in the analysis was 91.3; the lowest score was turned in by companies in the \$2 billion to \$5 billion revenue range.

By industry, the report found, airlines, electronics, natural gas, insurance, energy and regional banks turned in the worst FIN 48 compliance. Commodities, major drugs, consumer financial services, conglomerates, non-cyclical consumer products, investment services, capital goods, money center banks, computers and chemical manufacturing earned the highest overall compliance scores.

Audit Reform Committee Revises Yet Again

The Advisory Committee on the Auditing Profession has published its second draft of a report recommending changes to keep auditors afloat, but recommendations still offer an uncertain vision of what, if anything, to do about liability exposure.

The committee issued the second draft based on feedback from a first draft released in May and on further committee deliberations, according to committee member Gaylen Hansen, who is an audit partner with Colorado regional firm Ehrhardt Keefe Steiner & Hottman.



Hansen

Most notably, the second draft recommends that the Public Company Accounting Oversight Board establish an annual reporting requirement for large registered audit firms by 2011. Hansen says the committee heard strong views in favor of such reporting, although major audit firms disagree “on the grounds that it would not in their view contribute to audit quality.” The committee will continue to explore what should be required in such a filing and what benefit could be served by requiring annual filings, he adds.

The elephant still in the room, however, is whether audit firms should receive some cap on legal liability risks. The subcommittee mulling the issue so far has produced a discussion of the opposing views, but not a recommendation, Hansen says. “Those members that do not believe there is a sustainability threat believe that the firms have the primary responsibility for their own sustainability, and that it must be linked to conducting good audits,” he says.

Committee co-chair Don Nicolaisen, former chief accountant for the Securities and Exchange Commission, says the second draft is a “refinement” of the first draft and its addendum, without major revision to original positions.

The draft is open for comment for 30 days from its July 22 publication date.

IASB Overseer Proposes Governance Changes

The trustees overseeing the International Accounting Standards Board have proposed new governance changes, to make IASB more transparent and publicly accountable—and consequently make its global accounting standards more acceptable.

The Trustees of the International Accounting Standards Committee Foundation, which oversees IASB, has published a discussion document seeking feedback on its ideas for how IASB should expand by two members and answer to a monitoring group to enhance accountability.

Specifically, IASB’s overseer proposes to expand the Board from 14 to 16 members, and add guidelines that would specify geographic representation on the board. North America would receive four seats.

The trustees also propose establishing a monitoring group consisting of public authorities outside the IASC Foundation—namely, representatives of the European Commission, the International Monetary Fund, the International Organization of Securities Commissions, the Japan Financial Services Agency, the U.S. Securities and Exchange Commission, and the World Bank.

The monitoring group would oversee and approve the selection of trustees, establishing greater transparency and public accountability without impeding the independence of the standards-setting process.

The SEC has pointed to governance at IASB as a stumbling block to full U.S. adoption of International Financial Reporting Standards. IASB spokesman Mark Byatt says the changes spring partly from roundtable discussions on IASB governance, as well as a five-year constitutional review process undertaken by the trustees’ strategy committee.

“Given the number of jurisdictions that have adopted IFRS since the last constitutional review, it’s not surprising that trustees are proposing further enhancements to the public accountability of the IASB,” Byatt says.

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