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Definitions

- Financial Accounting Standards Board (FASB)
- American Institute of Certified Public Accountants (AICPA)
- Electronic health record (EHR)
- The 10th revision of the International Statistical Classification of Diseases and Related Health Problems (ICD-10)
- Office of Management and Budget (OMB) Circular
- US Generally Accepted Accounting Principles (US GAAP)
- Net patient service revenue (NPSR)
- Accounting Standards Codification (ASC)
- Technical Practice Aid (TPA)
- Not-for-profit (NFP)
- International Accounting Standards Board (IASB)
- Financial Reporting Executive Committee (FinREC)
- Health maintenance organizations (HMOs)
- Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Index
- Continuing care retirement communities (CCRCs)
- Securities and Exchange Commission (SEC)
- Public Company Accounting Oversight Board (PCAOB)
- Centers for Medicare & Medicaid Services (CMS)
Agenda

► Introductions

► Objectives

► Accounting Standard Updates (ASUs)

► FASB projects

► Other accounting and auditing matters
  ▶ American Taxpayer Relief Act of 2012
  ▶ Valuation of investments
  ▶ Implementation costs related to the ICD-10
  ▶ Modifications to auditor’s report

► Q&A and wrap-up
Objectives

► Our objectives are to gain an understanding the key Accounting Standards Updates (ASUs), FASB projects and other accounting and auditing matters that are currently impacting or will impact provider care organizations in the near future

► To cover practical matters relative to adoption of the new ASUs

► To understand the resources available to assist in further understanding the specifics related to the matters discussed within this presentation
Introductions

Brian Pavona - Audit Senior Manager – Chicago

Brian is a Senior Manager in Ernst & Young’s Midwest Assurance Health Sciences practice with over nine years experience leading health science audits, technical consultations, internal control assessments, and accounting and financial reporting educational updates. Clients serving/served include Actient Pharmaceuticals, Advocate Health care Network, Community Foundation of Northwest Indiana (d/b/a Community Health System), NantPharma, National Surgical Hospitals, National Surgical Care, Northwestern Community Hospital, NorthShore University HealthSystem, and Sagent Pharmaceuticals.

Lindsey Roe - Senior Manager and Americas Provider Care Industry Resident National Accounting – New York

Lindsey is a Senior Manager in Ernst & Young’s National Accounting Professional Practice group in New York. In her role as the firm’s Provider Care Industry Resident, she assists in writing the firm’s technical publications, leads educational sessions for both clients and audit professionals and participates in health care and not-for-profit accounting consultations. Lindsey is also responsible for creating and leading the firm’s Provider Care Accounting and Reporting Forum, which hosts approximately 20 EY clients in a quarterly round-table to discuss accounting topics. Clients serving/served include Indiana University Health, Inc., Parkview Health System, Inc., Bloomington Hospital, Inc., St. Mary Health System of America, Inc., and Saint Thomas Health Service, Inc.

Chris Thunander - Audit Manager – Chicago

Chris is a Manager in Ernst & Young’s Midwest Assurance Health Sciences practice with over five years experience in leading provider care, pharmaceutical and not-for-profit audits. Clients serving/served include Advocate Health care Network, Springfield Clinic, Community Foundation of Northwest Indiana, Indiana University Health, NorthShore University HealthSystem and Sagent Pharmaceuticals.
ASU 2010-23
Measuring Charity Care for Disclosure

► Effective for fiscal years beginning after 15 December 2010; retrospective application required

► Requires a provider to measure charity care costs using all direct and indirect costs

► Any reasonable estimation technique can be used but must be disclosed (e.g., cost-to-charge ratio)

► Cost shall not be reduced by reimbursement for charity care

► Reimbursement for charity care shall be disclosed

► FASB treatment of reimbursement for charity care in calculation not consistent with IRS Form 990 and many other public disclosures
Sample footnote disclosure:

“In the ordinary course of business, the Hospital provides services to patients who are financially unable to pay for hospital care. The Hospital includes charity care as a revenue deduction measured by the value of its services, based on standard charges, to patients who qualify under the Hospital’s charity care policy (typically those who meet certain minimum income guidelines and do not otherwise qualify for reimbursement under a governmental program). The estimated cost incurred by the Hospital to provide these services to patients who qualify for charity care was approximately $10.4 million and $13.2 million for the years ended December 31, 2011 and 2010, respectively. These estimates were determined using a ratio of cost-to-gross charges calculated from the Hospital’s most recently filed Medicare cost reports and applying that ratio to the gross charges associated with providing charity care for the period.”
Sample footnote disclosure from issued financial statements:

Example 1:

“In 2011 and 2012, $276,993 and $234,295, respectively, of patient charges has foregone under this policy. The system’s cost of providing charity care in 2011 and 2012 was $76,367 and $64,595, respectively. The cost of providing charity care is calculated using the 2010 Medicare cost-to-charge ratio.”
Sample footnote disclosure from issued financial statements:

Example 2:

“The Corporation adopted ASU 2010-23 for the fiscal period beginning January 1, 2011. This change requires that charity care be reported at estimated direct and indirect costs. The Corporation utilized a cost-to-charge ratio methodology for the cost analysis.

“Community commitment represents charity care and/or unreimbursed costs for services rendered at a reduced fee, or no fee, due to the inability of the patient to pay for services. The amount of the community commitment provided was approximately $6,860,000 and $9,656,000 for the years ended December 31, 2011 and 2010, respectively, at estimated cost. The decrease was partially caused by the uninsured discount-to-gross charges, as some of those discounts would previously have been captured as charity care write-offs. Additionally, as noted above, the Corporation used a cost-to-charge ratio methodology to estimate the cost of charity care, and this ratio has changed significantly over the prior year. The only reimbursement for charity care received by the Corporation is determined through a settlement process in the Hospital’s annual Medicare cost report filing. Charity Care reimbursement was approximately $4,149,000 and $372,000 for the years ended December 31, 2011 and 2010, respectively.”
ASU 2010-24
Presentation of Insurance Claims and Related Insurance Recoveries

► Effective for fiscal years and interim periods therein, beginning after 15 December 2010
► Applies to malpractice claims and similar contingent liabilities (e.g., workers’ compensation)
► Requires a gross-up of malpractice insurance claims and anticipated insurance recoveries
► If a difference exists between any liabilities and insurance recoveries, a cumulative adjustment should be recognized in opening unrestricted net assets in the period of adoption
► AICPA issued four TPAs (6400.49 – 6400.52) to address this guidance.
ASU 2010-29
Disclosure of Supplementary Pro Forma Information for Business Combinations

► Effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 15 December 2010; early adoption permitted

► Main provisions:
  ► The amendments in this update specify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only.
  ► The amendments clarify the acquisition date to be used.
  ► The amendments also improve the usefulness of the pro forma revenue and earnings disclosures by requiring a description of the nature and amount of material, nonrecurring pro forma adjustments that are directly attributable to the business combination(s).
ASU 2011-04
Amendments to Achieve Common Fair Value Measurements and Disclosures

► Preceded by ASU 2010-06, Improving Disclosures About Fair Value Measurements, which requires entities to:

► Disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measures and describe the reasons for the transfers

► Present separately, in the Level 3 reconciliation, information about purchases, sales, issuances and settlements (i.e., gross vs. net presentation)

► Clarify existing disclosure requirements:

► Provide fair value measurement disclosures for each class of assets and liabilities and reconciliation to statement of financial position

► Provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements (Level 2 and Level 3)

► Provide all fair value disclosures in one place (i.e., one footnote or summarized in one footnote)
ASU 2011-04
Amendments to Achieve Common Fair Value Measurements and Disclosures

ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and IFRS:

► Effective for fiscal years beginning after 15 December 2011. Non-public entities may apply the amendments early, but no earlier than for interim periods beginning after 15 December 2011.

► Amendments:
  ▶ Change the wording used to describe many of the requirements in US GAAP for measuring fair value and for disclosing information about fair value measurements
  ▶ Improve the comparability of fair value measurements presented and disclosed in financial statements prepared in US GAAP and International Financial Reporting Standards (IFRS)
  ▶ Change requirements for measuring fair value or disclosing information about fair value measurements
ASU 2011-07
Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts and the Allowance for Doubtful Accounts for Certain Health Care Entities

► Effective date:
  ► Effective for fiscal years and interim periods within those fiscal years beginning after 15 December 2011.
  ► Early adoption is permitted; retrospective application is required for all prior periods presented, except for disclosure requirements that are on a prospective basis only.

► Potential reversal of this guidance could occur in future years based on the FASB’s revenue recognition project currently underway (We will discuss in more detail in the FASB projects section of this presentation).
For health care entities that recognize a significant amount of NPSR at the time of service without assessing the patient’s ability to pay, the following is required:

- Disclosures regarding the timing and amount of uncollectible patient service revenue recognized as bad debts by major payor category
- Qualitative and quantitative disclosures about significant changes in the allowance for doubtful accounts
- Presentation in the statement of operations of the provision for bad debts shown as a deduction from NPSR
- Disclosures regarding its policy for assessing collectability in determining the timing and amount of NPSR to be recognized by major payor category
- Disclosures of its patient service revenue, net of contractuals and discounts, before the provision for bad debts, by major payor category
ASU 2011-07

Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts and the Allowance for Doubtful Accounts for Certain Health Care Entities

Current income statement format

<table>
<thead>
<tr>
<th>Revenue</th>
<th>December 31</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2011</td>
<td>2010</td>
<td></td>
</tr>
<tr>
<td>Net patient service revenue</td>
<td>$673,479</td>
<td>$629,448</td>
<td></td>
</tr>
<tr>
<td>Premium revenue</td>
<td>224,458</td>
<td>248,821</td>
<td></td>
</tr>
<tr>
<td>Other operating revenue</td>
<td>23,489</td>
<td>21,907</td>
<td></td>
</tr>
<tr>
<td>Net assets released from restrictions</td>
<td>1,440</td>
<td>1,256</td>
<td></td>
</tr>
<tr>
<td><strong>Total revenue</strong></td>
<td><strong>922,866</strong></td>
<td><strong>901,432</strong></td>
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</tr>
</tbody>
</table>

Operating expenses

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2010</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Salaries and wages</td>
<td>320,370</td>
<td>295,289</td>
<td></td>
</tr>
<tr>
<td>Employee benefits</td>
<td>97,189</td>
<td>86,096</td>
<td></td>
</tr>
<tr>
<td>Supplies and drugs</td>
<td>167,604</td>
<td>163,345</td>
<td></td>
</tr>
<tr>
<td>Professional fees and purchased services</td>
<td>170,735</td>
<td>180,180</td>
<td></td>
</tr>
<tr>
<td><strong>Bad debts</strong></td>
<td><strong>48,162</strong></td>
<td><strong>44,412</strong></td>
<td></td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>50,126</td>
<td>37,890</td>
<td></td>
</tr>
<tr>
<td>Interest</td>
<td>11,716</td>
<td>6,079</td>
<td></td>
</tr>
<tr>
<td>Other expenses</td>
<td>55,302</td>
<td>57,080</td>
<td></td>
</tr>
<tr>
<td><strong>Total operating expenses</strong></td>
<td><strong>$921,204</strong></td>
<td><strong>$870,371</strong></td>
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</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2010</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating income</td>
<td>1,662</td>
<td>31,061</td>
<td></td>
</tr>
<tr>
<td>Operating margin</td>
<td>0.18%</td>
<td>3.45%</td>
<td></td>
</tr>
</tbody>
</table>
### ASU 2011-07

*Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts and the Allowance for Doubtful Accounts for Certain Health Care Entities*

### Revised income statement format

<table>
<thead>
<tr>
<th></th>
<th>December 31</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2011</td>
<td>2010</td>
<td></td>
</tr>
<tr>
<td><strong>Revenue</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Patient service revenue</td>
<td>$673,479</td>
<td>$629,448</td>
<td></td>
</tr>
<tr>
<td><strong>Less provision for doubtful accounts</strong></td>
<td>(48,162)</td>
<td>(44,412)</td>
<td></td>
</tr>
<tr>
<td>Patient service revenue, net</td>
<td>625,317</td>
<td>585,036</td>
<td></td>
</tr>
<tr>
<td>Premium revenue</td>
<td>224,458</td>
<td>248,821</td>
<td></td>
</tr>
<tr>
<td>Other operating revenue</td>
<td>23,489</td>
<td>21,907</td>
<td></td>
</tr>
<tr>
<td>Net assets released from restrictions</td>
<td>1,440</td>
<td>1,256</td>
<td></td>
</tr>
<tr>
<td><strong>Total revenue</strong></td>
<td>874,704</td>
<td>857,020</td>
<td></td>
</tr>
<tr>
<td><strong>Operating expenses</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries and wages</td>
<td>320,370</td>
<td>295,289</td>
<td></td>
</tr>
<tr>
<td>Employee benefits</td>
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<td>180,180</td>
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<td>Depreciation and amortization</td>
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<td>37,890</td>
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</tr>
<tr>
<td>Interest</td>
<td>11,716</td>
<td>6,079</td>
<td></td>
</tr>
<tr>
<td>Other expenses</td>
<td>55,302</td>
<td>57,080</td>
<td></td>
</tr>
<tr>
<td><strong>Total operating expenses</strong></td>
<td>873,042</td>
<td>825,959</td>
<td></td>
</tr>
<tr>
<td>Operating income</td>
<td>1,662</td>
<td>31,061</td>
<td></td>
</tr>
<tr>
<td>Operating margin %</td>
<td>0.19%</td>
<td>3.62%</td>
<td></td>
</tr>
</tbody>
</table>
Sample footnote from ASC 954-605-55:

“The Hospital recognizes patient service revenue associated with services provided to patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients who do not qualify for charity care, the Hospital recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy). On the basis of historical experience, a significant portion of the Hospital’s uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Hospital records a significant provision for bad debts related to uninsured patients in the period the services are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the period from these major payor sources is as follows.”
Sample footnote from ASC 954-605-55:

“The Hospital’s allowance for uncollectible accounts for self-pay patients increased from 76% of self-pay accounts receivable at December 31, 2011, to 85% of self-pay accounts receivable at December 31, 2012. The increase in the allowance rates is attributable to the deterioration in the local economy, which has led to increased self-pay and Medicaid pending accounts receivable, and the increase in the co-insurance and deductible amounts due from patients. In addition, the self-pay write-offs decreased $5,315,000 from $35,939,000 in 2011 to $30,624,000 in 2012, due to the increased charity care write-offs during the year. The Hospital does not maintain a material allowance for uncollectible accounts from third-party payors, nor did it have significant write-offs from third-party payors.”
ASU 2011-07
Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts and the Allowance for Doubtful Accounts for Certain Health Care Entities

Implementation guidance:

► FASB staff provided its views on how a consolidated health care system should adopt ASU 2011-07 when some subsidiaries recognize a significant amount of NPSR at the time of service, without assessing the patient’s ability to pay, and others do not.

► The determination of whether the presentation of bad debts at the consolidated reporting entity level should be based on an entity-wide assessment of significance or on significance determined at the level of each individual subsidiary is an accounting policy election.

► This must be applied consistently and disclosed.

► AICPA issued a TPA (6400.47) to address this guidance.
ASU 2011-08
Testing Goodwill for Impairment

► Optional qualitative assessment to determine if traditional two-step approach is necessary
► Effective for all fiscal years beginning after 15 December 2011, with early adoption permitted
► May change how a company tests for impairment, but should not change timing of annual assessment
► Goal is to reduce cost and complexity of testing goodwill for impairment
► Does not apply to other intangible assets
► Additional disclosures regarding the qualitative factors that were considered
Key points:

- Qualitative assessment of whether it is more likely than not (a greater than 50% chance) that a reporting unit’s fair value is less than its carrying amount.
- Includes an unconditional option to use or bypass the qualitative assessment for any reporting unit in any period.
- Eliminates option to carry forward fair value calculations from prior years.
- Generally requires significant documentation in year one.
**ASU 2011-08**  
*Testing Goodwill for Impairment: How the impairment tests compare*

<table>
<thead>
<tr>
<th><strong>Current</strong></th>
<th><strong>New guidance</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Step 1</strong></td>
<td><strong>Step 1</strong></td>
</tr>
<tr>
<td>Compare fair value of reporting unit to carrying value, including goodwill*</td>
<td>Compare fair value of reporting unit to carrying value, including goodwill*</td>
</tr>
<tr>
<td><strong>Step 2</strong></td>
<td><strong>Step 2</strong></td>
</tr>
<tr>
<td>Determine amount of goodwill impairment, if any</td>
<td>Determine amount of goodwill impairment, if any</td>
</tr>
</tbody>
</table>

Qualitative assessment: Evaluate qualitative factors to determine likelihood of carrying value exceeding fair value

*A reporting unit with a zero or negative carrying value is required to perform the qualitative assessment in place of this step of the impairment test. If the company concludes that it is more likely than not that impairment exists after performing the qualitative assessment, it would proceed directly to Step 2 of the impairment test.*
None of these factors by themselves is determinative. Rather, a company should consider the significance of each adverse factor as well as the existence of any positive or mitigating events.
Polling Question

Do you plan to use the qualitative assessment in the current year to begin your process of evaluating goodwill for possible impairment?

A. Yes  
B. No  
C. Not applicable
ASU 2012-01
Continuing Care Retirement Communities — Refundable Advance Fees

► Clarifies that an entity should classify an advance fee as deferred revenue when a continuing care retirement community has a resident contract that provides for payment of the refundable advance fee upon re-occupancy by a subsequent resident, which is limited to the proceeds of re-occupancy. Refundable advance fees that are contingent upon re-occupancy by a subsequent resident but are not limited to the proceeds of re-occupancy should be accounted for and reported as a liability.

► For public entities (including conduit bond obligors), this ASU is effective for fiscal periods beginning after 15 December 2012. For nonpublic entities, this ASU is effective for fiscal periods beginning after 15 December 2013. Early adoption is permitted.

► Adoption should be applied retrospectively by recording a cumulative-effect adjustment to opening retained earnings (or unrestricted net assets) as of the beginning of the earliest period presented.
Optional qualitative assessment to determine if traditional two-step approach is necessary, similar to qualitative assessment for goodwill.

Effective for all fiscal years beginning after 15 September 2012, with early adoption permitted.

May change how a company tests for impairment, but should not change timing of annual assessment.

Using the new qualitative assessment will require significant judgment.

Companies that use the qualitative assessment will have to consider positive and negative evidence that could affect the significant inputs used to determine fair value.
Objective of this update is for an NFP to classify cash receipts from the sale of donated financial assets consistently with cash donations received in the statement of cash flows if those cash receipts were from the sale of donated financial assets that upon receipt were directed without the NFP imposing any limitations for sale and were converted nearly immediately into cash.

Effective prospectively for fiscal years, and interim periods within those years, beginning after 15 June 2013. Retrospective application to all prior periods presented upon the date of adoption is permitted. Early adoption from the beginning of the fiscal year of adoption is permitted.
FASB projects
Joint projects overview

► FASB and IASB goal: improved, high-quality, converged accounting standards
► Boards have focused on financial instruments, revenue recognition, leases and insurance contracts
  ► Timelines were extended
  ► Decisions to re-expose revenue and leases proposals caused more delays
  ► Certain lower-priority projects set aside for near term
  ► Completing revenue recognition in the first half of 2013 is a priority
  ► Several exposure drafts (EDs) expected in the first half of 2013
► Boards are redeliberating many projects; making tentative decisions
  ► Decisions are subject to change as the redeliberations progress
► Effective dates and transition methods for several joint projects have not been finalized
Joint projects timeline

<table>
<thead>
<tr>
<th>Active projects</th>
<th>2010—2011 (highlights of prior activity)</th>
<th>Q1—Q3 2012</th>
<th>Q4 2012</th>
<th>Q1—Q2 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Instruments</td>
<td></td>
<td></td>
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<tr>
<td>Classification and measurement</td>
<td>FASB ED</td>
<td>ED^2</td>
<td>ED</td>
<td>ED</td>
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<tr>
<td></td>
<td>IASB Final^3</td>
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<tr>
<td>Impairment</td>
<td>IASB ED</td>
<td>SD</td>
<td>ED</td>
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<tr>
<td></td>
<td>FASB ED</td>
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<td>ED</td>
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<tr>
<td>Hedging</td>
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<td>Review draft</td>
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<tr>
<td></td>
<td>FASB DP</td>
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<td>Final^6</td>
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<tr>
<td>Revenue Recognition</td>
<td>FASB ED</td>
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<td>Final</td>
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<td></td>
<td>IASB ED</td>
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<td></td>
<td>Final</td>
</tr>
<tr>
<td>Leases</td>
<td>FASB ED</td>
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<td></td>
<td>ED</td>
</tr>
<tr>
<td></td>
<td>IASB ED</td>
<td></td>
<td></td>
<td>ED</td>
</tr>
<tr>
<td>Insurance Contracts</td>
<td>FASB DP</td>
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<td></td>
<td>ED</td>
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<tr>
<td></td>
<td>IASB ED</td>
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<td>Consolidation</td>
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</tr>
<tr>
<td></td>
<td>IASB ED</td>
<td></td>
<td></td>
<td>Final</td>
</tr>
</tbody>
</table>

ED — Exposure draft RT — Roundtable SD — Supplementary document DP — Discussion paper

1 The FASB issued a single comprehensive proposal on all three phases of this project.
2 In Q2 2012, the FASB separately issued an ED on liquidity and interest rate risk disclosures related to financial instruments.
3 The IASB’s final IFRS on classification and measurement for liabilities. In 2011, the IASB deferred the mandatory effective date of IFRS 9.
4 The IASB’s project is to undertake limited scope changes to IFRS 9.
5 The IASB expects to issue a separate DP on macro hedge accounting in 2013.
6 In Q2 2012, the IASB issued amendments to clarify the transition guidance in IFRS 10.
7 In Q4 2012, the FASB proposed a scope clarification.
8 In Q1 2013, the FASB is expected to issue a standard that would require enhanced disclosures about items reclassified out of accumulated other comprehensive income.
9 Further action by the FASB on these projects is not expected in the near term.

Note: Our timeline for some FASB projects is based on discussions with staff and may differ from the technical plan on the FASB website.

Recently completed projects
- Balance Sheet — Offsetting
- Statement of Comprehensive Income
- Fair Value Measurement

Inactive projects
- Financial Statement Presentation
- Financial Instruments with Characteristics of Equity
- Emissions Trading Schemes
FASB projects - Revenue recognition
Overview

► New joint revenue recognition ED would replace existing US GAAP and IFRS for revenue recognition
  ► Virtually every industry would be affected
  ► Leases, insurance contracts, financial instruments, guarantees and certain nonmonetary transactions would be out of scope
► Certain aspects of the proposed model would result in a significant change from current practice
► Redeliberations planned for July 2012 through early 2013
  ► Final standard expected in Q2-Q3 of 2013
► Effective date and transition
  ► Effective date has been tentatively set for fiscal years beginning on or after 1 January 2017
  ► Retrospective application would be required, with some practical expedients
FASB projects - Revenue recognition
Summary of proposed model

1. Identify the contract(s) with the customer
2. Identify the separate performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price to the separate performance obligations
5. Recognize revenue when each performance obligation is satisfied
In November 2012, the FASB and the IASB tentatively decided that the effects of customer credit risk (i.e., bad debt expense) would be presented as a separate line item in operating expense rather than adjacent to revenue.

If the Boards include this approach in a final standard, entities that record patient service revenue at the time of service without assessing the patient’s ability to pay would be required to change their presentation of the provision for bad debts.

The Boards plan to continue re-deliberations on their 2011 revenue recognition proposal next year. They are targeting the first half of 2013 for issuing a final standard.

Proposed effective date is periods beginning on or after 1 January 2017.

The guidance in ASU 2011-07 remains effective until any new standard is issued.
In June 2012, the FASB proposed requiring all entities — public, private and not-for-profit — to provide quantitative and qualitative liquidity risk disclosures in their audited financial statements.

The proposal would require significant effort by preparers to provide the disclosures, which would be required to be audited.

Public entities would provide these disclosures both annually and quarterly. Nonpublic entities would be required to provide the disclosures annually.
In February 2013, the FASB issued its classification and measurement exposure draft.

The proposal would apply to all entities across all industries, including health care and not-for-profit sectors.

Comments are due 15 May 2013.
FASB projects – Financial instruments
Classification and measurement

Key changes from current US GAAP would include:

- Debt instruments (including loans) classified and measured in one of three categories based on the instrument’s cash flow characteristics and an entity’s business model for managing the instrument.
- Reclassifications required only when an entity’s business model for managing its financial assets changes (no “tainting” notion).
- Equity investments measured at fair value through net income (FV-NI), unless they qualify for certain exceptions.
- Equity method investments held for sale at initial qualification being measured at FV-NI.
- Elimination of today’s embedded derivative bifurcation requirements for hybrid financial assets.
- Limitation on the use of the fair value option.
- Expanded presentation and disclosure requirements.
FASB projects - Leases
Overview

► Boards issued joint ED in 2010
  ► Objective: record lease contracts on balance sheet
  ► Responded to some of the criticisms of current model
  ► Addressed perspective of lessees and lessors

► Boards decided to re-expose due to significant changes to proposed model
  ► Second ED expected in the first quarter of 2013

► No effective date has been determined yet
► Full retrospective or modified retrospective adoption at the effective date would be required
► Lessees and lessors could elect to apply current operating lease accounting for short-term leases
FASB projects - Leases
Tentative decisions

- Lessees and lessors would distinguish between two types of leases based primarily on the nature of the underlying asset being leased
  - Certain conditions could overcome presumptive classification
  - Premise for classification is whether the lessee acquires and consumes more than an insignificant portion of the underlying asset over the lease term
- Lessees would recognize a right-of-use asset and a lease liability for both types of leases
  - Leases of property (i.e., land, building or part of a building) – generally recognize straight-line lease expense similar to operating leases under current accounting
  - Leases of assets other than property (e.g., equipment) – generally recognize amortization expense and interest expense separately in a pattern usually resulting in accelerated expense recognition
- Lessors
  - Leases of property – generally apply operating lease accounting
  - Leases of assets other than property – generally recognize a lease receivable, a residual asset and day-one profit (if any)
    - Income related to interest on the receivable and accretion of residual asset would be recognized over lease term
FASB projects - Leases
Tentative decisions (continued)

► Initially measure lessee’s liability and lessor’s receivable at the present value of the lease payments to be made over the lease term
► Lease term: noncancelable period plus any options for which there is significant economic incentive to extend (or not terminate) lease
  ▶ Examples – renewal rates priced at a bargain or penalty payments
► For a purchase option with significant economic incentive to exercise, include exercise price in lease payments
  ▶ Lessees would amortize right-of-use asset over economic life of underlying asset
► Contingent rents based on:
  ▶ An index or rate would be included in lease payments
  ▶ Performance or usage would not be included in lease payments – instead, they would be recognized when incurred
► Residual value guarantees
  ▶ Lessees would recognize amounts expected to be payable as lease payments
  ▶ Lessors would not recognize amounts expected to be received until the end of the lease
FASB projects - Leases
Tentative decisions (continued)

► Non-lease components would be accounted for separately except in limited circumstances

► Reassessment required for:
  ► Lease term and purchase option when there is a significant change in factors relevant to determining whether a significant economic incentive exists
    ► Changes in market rates after lease begins would not be included in assessment
  ► Discount rate when there is a change in lease payments due to a change in the assessment of the lease term
  ► Residual value guarantees when events or circumstances indicate a significant change in the amount expected to be payable (lessees only)
  ► Contingent rents based on an index or rate reassessed each reporting period using index or rate that exists at the end of each reporting period

► Assess for impairment of the lessee’s right-of-use asset and lessor’s receivable and residual asset

► Sale-leaseback transactions
  ► Would be assessed using revenue recognition guidance
  ► Certain conditions would indicate that a sale has not occurred
    ► Would require the transaction to be accounted for as a financing
Polling Question

Have you begun your assessment of how the FASB’s lease project will impact your organization?

A. Yes  
B. No  
C. Not applicable
## FASB projects – Private company framework

**Actions taken at second meeting of the Private Company Council in February 2013:**

<table>
<thead>
<tr>
<th>Private company decision-making framework</th>
<th>Next steps</th>
</tr>
</thead>
<tbody>
<tr>
<td>► FASB and PCC made changes to staff recommendations:</td>
<td>► Framework is expected to be finalized later this year</td>
</tr>
<tr>
<td>▶ Presumption that industry-specific guidance is relevant was removed</td>
<td>► In the interim:</td>
</tr>
<tr>
<td>▶ Clarification that “all or nothing approach” would not be required</td>
<td>▶ The PCC and FASB will consider exceptions and modifications to US GAAP</td>
</tr>
<tr>
<td>▶ Clarifications of the “red flag” approach</td>
<td>▶ Work continues on a single definition of a non-public entity (private company)</td>
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<td>► Exposure draft on revised framework expected in March</td>
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</tbody>
</table>
# FASB projects – Private company framework

<table>
<thead>
<tr>
<th>Topics selected for initial agenda</th>
<th>Research initiatives</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recognizing and measuring, at fair value, various identifiable intangible assets (other than goodwill) acquired in business combinations</td>
<td>Stock-based compensation</td>
</tr>
<tr>
<td>Consolidating variable interest entities</td>
<td>Development-stage enterprises</td>
</tr>
<tr>
<td>Accounting for “plain vanilla” interest-rate swaps with single counterparties</td>
<td>Accounting for interest-rate swaps with multiple counterparties</td>
</tr>
</tbody>
</table>

*The PCC decided not to further pursue accounting for uncertain tax positions*
FASB projects – Discontinued operations

► In January 2013, the FASB decided to propose a new definition of a discontinued operation that would raise the threshold to qualify (e.g., a separate major line of business or major geographical area) and permit an increased level of ongoing involvement (e.g., allow for continuing cash flows and significant continuing involvement).

► The FASB tentatively decided to require disclosures about discontinued operations and about certain individually material disposal transactions that do not meet the definition of a discontinued operation.

► The FASB directed its staff to draft a proposal as soon as possible.
Other accounting and auditing matters
American Taxpayer Relief Act of 2012

► Commonly known as the fiscal-cliff legislation, this bill was signed into law by President Obama on 3 January 2013

► Included several Medicare related changes:
  ► Extended the Medicare Dependent Hospital program (retroactive to 1 October 2012)
  ► Amended the Medicare Low Volume Hospital program (retroactive to 1 October 2012)
  ► Extended the claw-back period for Medicare Administrative Contractors to collect on errors in payment from 3 years to 5 years
    ▶ This provision has not yet been enacted in Medicare rules and regulations
Valuation of investments

- Regulators at the SEC and the PCAOB (and the AICPA/peer reviews for non-issuers) have increased their focus on companies’ use of fair value information obtained from third-party pricing sources, particularly for securities for which there is a limited market (i.e., Level 2).

- The expectation is that companies and their auditors understand the valuation models, assumptions and inputs used by third-party pricing sources to determine the fair value of securities.

- Companies need to evaluate their understanding of fair value information obtained from third-party pricing sources. This will require an update to documentation (i.e., policies, procedures and controls).
Considerations when estimating uncertainty:

- Inquiries and documentation related to service provider pricing sources
- Inquiries related to key characteristics of fixed-income securities
- Market transaction support for fixed-income securities that are considered to have a higher estimation uncertainty
Valuation of investments
Inputs and assumptions

- Contractual cash flow structure (e.g., senior vs. subordinate)
- Interest rate (e.g., floating vs. fixed)
- Liquidity (e.g., frequency of transactions)
- Period to maturity
- Credit rating (e.g., AAA, BBB)
- Collateral (e.g., prime vs. subprime)
- Prepayment risk
- Conversion features (e.g., convertible vs. straight debt)
ICD-10 implementation costs

Accounting for costs associated with ICD-10:

Entities should consider the applicable guidance based on their facts and circumstances:

- ASC 720-45, Other Expenses – Business and Technology Reengineering
- ASC 350-40, Internal-Use Software
- Costs associated with training or consultations should be expensed as incurred

Given the potential materiality, entities should consider disclosing the treatment of these costs in the notes to the financial statements.

The AICPA HealthCare Expert Panel has issued a TPA (6400.48) on this topic.
Modification of auditor’s report

In 2012, the AICPA redrafted their standards for reporting on audits of financial statements for non-issuers and issued new clarified standards.

- Requires the use of headings throughout the auditor’s report to clearly distinguish each section of the report.
- Expands the description in the auditor’s report of management’s responsibility for the preparation and fair presentation of the financial statements.
- Provides a new section of the report for reporting on other legal and regulatory requirements, when applicable.
- The clarified standard introduces the terms “emphasis-of-matter” and “other-matter” paragraphs. Emphasis-of-matter paragraphs are intended to draw users’ attention to a matter, and other-matter paragraphs are intended to communicate a matter.
Ernst & Young resources

► AccountingLink
► Global Accounting and Auditing Information Tool (GAAIT)
► Technical lines
► To the Point publications
Polling Question

Were the objectives of today’s webcast met?
A. Yes
B. No