

**MEMO# 8900**

May 16, 1997

## **AICPA PROPOSAL LIMITING ORGANIZATION COSTS**

May 16, 1997 TO: ACCOUNTING/TREASURERS COMMITTEE No. 13-97 UNIT INVESTMENT TRUST COMMITTEE No. 31-97 RE: AICPA PROPOSAL LIMITING ORGANIZATION COSTS

The Accounting Standards Executive Committee of the AICPA recently issued an exposure draft of a proposed statement of position Reporting on the Costs of Start-up Activities. The proposed SOP would apply to all entities that prepare financial statements in conformity with generally accepted accounting principles, including investment companies. The proposed SOP would require costs associated with pre-operating "start-up activities" to be expensed as incurred and would limit the types of costs that can be capitalized as organization costs. In the context of investment companies, the proposed SOP would effectively require the adviser or sponsor to bear certain organization costs which are currently born by the fund. A summary of the proposed SOP is set forth below. Copies of the proposed SOP may be obtained by writing to the AICPA Order Department, Harborside Financial Center, 201 Plaza Three, Jersey City, NJ 07311-3881 or by visiting the AICPA's internet website at [aicpa.org](http://aicpa.org). The comment deadline is July 22, 1997. Proposed SOP The proposed SOP requires that costs of start-up activities be expensed as incurred. Start-up activities are defined broadly as those one-time activities related to opening a new facility, introducing a new product or service, conducting business in a new territory, conducting business with a new class of customer or beneficiary, initiating a new process in an existing facility, or commencing some new operation. Start-up activities relate to the period before an entity commences operations or production and after operations have begun, but before normal productive capacity is reached. The proposed SOP defines organization costs as the costs of preparing: (1) the entity charter; (2) the partnership agreement; (3) the bylaws; (4) the minutes of organizational meetings; and (5) the terms of original stock certificates. Consistent with current practice, these costs may be capitalized as an asset and amortized to expense over a period not to exceed 60 months. However, certain costs typically treated as organization costs by investment companies fall outside the definition contained in the proposed SOP. For example, costs of legal services associated with preparing the initial registration statement, administration, custody, and transfer agent agreements, as well as audit fees relating to the initial seed capital statement of assets and liabilities would not be treated as organization costs under the proposed SOP. The proposed SOP would be effective for financial statements for fiscal years beginning after December 15, 1997. Initial application of the SOP should be reported as the cumulative effect of a change in accounting principle, as described in Accounting Principles Board Opinion No. 20, Accounting Changes. Initial application of the SOP should be as of the beginning of the fiscal year in which the SOP is first adopted. In the Basis for Conclusions section of the proposed SOP AcSEC indicates that no evidence has been identified that demonstrates a

direct causal relationship between start-up costs incurred and related future economic benefits; therefore, those costs should be expensed as incurred. The proposed SOP notes that AcSEC considered requiring capitalization and amortization of the costs of start-up activities, since these costs are undertaken with an expectation that there will be future benefits. However, AcSEC concluded that, similar to research and development costs, start-up costs should be expensed as incurred. The comment deadline on the proposed SOP is July 22. However, the AICPA Investment Companies Committee plans to meet with AcSEC during the week of June 9 to clear the Investment Company Audit Guide. One of the issues to be addressed with AcSEC at the June meeting is organization costs. The Institute would like to submit its comment letter on the proposed SOP prior to the June AcSEC meeting. Accordingly, if you have any comments on the proposed SOP that you would like to be included in an Institute comment letter please contact the undersigned at 202/326-5851 or [smith@ici.org](mailto:smith@ici.org). by June 2. Gregory M. Smith Director - Operations/ Compliance & Fund Accounting

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