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## From the authors

In this update, we share recent financial reporting developments from the Securities and Exchange Commission (SEC), the Public Company Accounting Oversight Board (PCAOB), and the Center for Audit Quality (CAQ).

December brings the annual American Institute of Certified Public Accountants (AICPA) National Conference on SEC and PCAOB Developments. Representatives of the SEC, the PCAOB, and the CAQ provide their perspectives on accomplishments and priorities for the coming year. Not surprisingly, themes from this year's conference included the importance of accountants and independent auditors in forming the foundation of our capital markets, the role of the audit committee, the implementation of new accounting and auditing standards, and the slate of rulemaking and regulatory changes on the horizon.

As 2020 arrives, the SEC remains focused on the three key prongs of its strategic plan and executing on its rulemaking agenda. The PCAOB is focused on implementing newly effective and upcoming rules including critical audit matters (CAMs), auditing estimates, and use of specialists as well as revamping its inspection program and continuing stakeholder engagement. The CAQ continues to foster audit quality to increase investor confidence through a variety of mechanisms.

We hope you find this information useful, and we welcome your feedback.

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## From the SEC

### Strategic plan and SEC leadership priorities

#### Strategic plan

The SEC's [current](#) strategic plan features three goals:

- “Focus on the long-term interests of our Main Street investors. ... Initiatives under this goal will include modernizing disclosure and expanding investor choice.”
- “Recognize significant developments and trends in our evolving capital markets and adjust our efforts to ensure we are effectively allocating our resources. ... by analyzing market developments, evaluating existing rules and procedures, understanding the continually changing cyber-landscape and ensuring the appropriate resources are dedicated to each area.”
- “Elevate the SEC’s performance by enhancing our analytical capabilities and human capital development. The SEC will invest in data and technology.”

#### SEC leadership priorities

The 2019 AICPA National Conference on SEC and PCAOB Developments (AICPA conference), which occurred on Dec. 9-11, 2019, in Washington, D.C., provided a forum for SEC leadership to present accomplishments for the year and help participants understand the SEC’s current priorities.

#### Focus of the chair and chief accountant

Day one of the AICPA conference featured a joint discussion with Chair Jay Clayton and Chief Accountant Sagar Teotia. The discussion addressed multiple topics including the significant role accountants and auditors play in supporting capital formation while at the same time protecting investors. Other key topics included the importance of audit committees, reference rate reform, non-generally accepted accounting principles (GAAP) measures, and the implementation of new accounting standards.

Teotia also participated in a panel discussion with two members of the SEC’s Office of the Chief Accountant (OCA), which covered highlights of the OCA’s current priorities including:

- Engagement with stakeholders
- Oversight of the Financial Accounting Standards Board (FASB); implementation of new accounting standards and current FASB standard-setting
- Oversight of the PCAOB
- International accounting, audit, and disclosure matters
- Staff guidance and other initiatives
- Other significant areas of focus such as internal control over financial reporting (ICFR), audit committees, and technology and innovation

Concurrent with the conference, the staff released a [prepared statement](#) summarizing the panel’s remarks.

## Focus of the Division of Corporation Finance

Division of Corporation Finance (Corp Fin) Director Bill Hinman covered a wide range of issues in his moderated remarks including:

- Corp Fin's rulemaking agenda for the coming year, which is focused on balancing capital formation with investor protection, and the status of current rule proposals.
- Disclosure of emerging risks such as reference rate reform, cybersecurity, Brexit, and sustainability. Hinman indicated a good principle is to consider all forums where an entity addresses an issue and consider how that might affect an entity's disclosure documents. While the staff is not broadly issuing comments on emerging risk disclosures, the staff is currently monitoring disclosure in this area. Moreover, if an entity has identified a material risk, the staff expects disclosure about board oversight of the risk, but the staff believes entities can improve in this area.
- The impact of stock buybacks on an entity's compensation discussion and analysis disclosure.
- Accounting for digital assets.

Following are additional details of the key priorities of the chair, the chief accountant, and Corp Fin most relevant to public companies.

## A deeper dive on SEC leadership priorities

### Importance of audit committees

#### Perspectives of SEC leadership

Both Chair Clayton and Chief Accountant Teotia remarked upon the importance of audit committees including how auditor independence is the shared responsibility of the audit committee, how audit committees were involved in successful implementations of the major accounting standards, how the tone of the audit committee affects the organization, and the chair's view that the greatest investor "bang for the buck" was the *Sarbanes-Oxley Act of 2002* mandate for independent audit committees.

#### Statement on audit committee's role in financial reporting

On Dec. 30, 2019, SEC leadership (SEC Chairman Clayton, Chief Accountant Teotia, and Corp Fin Director Hinman) issued "[Statement on Role of Audit Committees in Financial Reporting and Key Reminders Regarding Oversight Responsibilities.](#)"

The statement provides observations and reminders on potential focus areas for audit committees for the 2019 calendar year-end financial reporting process. These observations and reminders are intended to assist audit committees in carrying out their oversight role, including promoting efficient and constructive dialogue on the focus areas between audit committees, management, and independent auditors. The scope of an audit committee's work is broad and includes a variety of important responsibilities, and these observations and reminders are not intended to reflect a comprehensive list.

General observations regarding financial reporting and auditing highlighted in the statement include tone at the top, auditor independence, GAAP, ICFR, and independent auditor communications with audit committees. The statement also discusses non-GAAP measures, reference rate reform, and CAMs.

## Auditor independence

### **Proposal to codify certain consultations and modernize auditor independence rules**

On Dec. 30, 2019, the SEC announced proposed rule amendments to codify certain staff consultations and update certain aspects of its auditor independence framework. To address the significant changes in the capital markets and those who participate in them, the amendments would update certain aspects of the auditor independence rule set to more effectively structure the independence rules and analysis so that relationships and services that would not pose threats to an auditor's objectivity and impartiality do not trigger nonsubstantive rule breaches or potentially time-consuming audit committee review of nonsubstantive matters.

### **OCA remarks at the AICPA conference**

Vassilios Karapanos, associate chief accountant, provided additional details on the staff's auditor independence work in 2019 including an [overview](#) of the SEC's new final rule on lending relationships and auditor independence and recently updated [staff guidance](#) on frequently asked independence questions.

### **Auditor independence for certain lending relationships**

The SEC [adopted](#), on June 18, 2019, a [final rule](#), "Auditor Independence With Respect to Certain Loans or Debtor-Creditor Relationships," that amends the SEC's auditor independence rules when the auditor has a lending relationship with certain shareholders of an audit client at any time during an audit or professional engagement period under Rule 2-01(c)(1)(ii)(A) of Regulation S-X (the Loan Provision). The amendments will do the following:

- Focus the analysis on beneficial ownership rather than on both record and beneficial ownership.
- Replace the existing 10% bright-line shareholder ownership test with a "significant influence" test.
- Add a "known through reasonable inquiry" standard for identifying beneficial owners of the audit client's equity securities.
- For the definition of "audit client" for a fund under audit, exclude any other funds that otherwise would be considered affiliates of the audit client under the rules for certain lending relationships.

The amendments were effective Oct. 3, 2019.

## Implementation of new accounting standards

### **OCA remarks at the AICPA conference**

Various members of OCA staff delivered prepared speeches at the AICPA conference, and several of the speeches addressed the staff's involvement with consultations during the past year on new accounting standards. Speakers and topics included:

- Lauren K. Alexander, professional accounting fellow – [remarks](#) on revenue recognition consultations, specifically principal versus agent guidance, and observations from a current expected credit losses consultation
- Aaron Shaw, professional accounting fellow – [remarks](#) on revenue recognition for a sale and leaseback transaction and determination of whether a registrant is the primary beneficiary of a variable interest entity
- Jamie N. Davis, professional accounting fellow – [remarks](#) on discontinuation of the London Interbank Offered Rate (LIBOR), including effects on cash flow hedges, efforts of the FASB to address the discontinuation of LIBOR, and amendments to equity-classified preferred stock instruments that use LIBOR
- Erin Bennett, professional accounting fellow – [remarks](#) on application of equity method accounting, implementation of the new lease accounting standard, and collectability of lease payments
- Susan M. Mercier, professional accounting fellow – [remarks](#) on revenue recognition consultations, specifically related to identification of performance obligations

## Disclosure of the impact of recently issued accounting standards (SAB 74)

Kevin Vaughn, senior associate chief accountant, on Sept. 9, 2019, provided thoughts on Staff Accounting Bulletin (SAB) 74 disclosures for the current expected credit losses (CECL) standard including:

- Management should share what they know when they know it under SAB 74.
- Investors want to know the impact to the financial statements and an estimated range with an explanation for why the company cannot provide a more accurate estimate to help investors prepare for the Jan. 1 adoption for SEC filers that are not smaller reporting companies (SRCs).
- The expectation is not that entities will wait to disclose the impact of CECL until the entity has a precise number.
- Entities should plan what information will be shared with investors post-adoption.

## Oversight of the PCAOB and international matters

### OCA remarks at the AICPA conference

Staff members in OCA provided various perspectives on how the SEC oversees the PCAOB, including implementation of new PCAOB standards, as well as how the staff monitors international audit standard setting:

- Louis J. Collins, professional accounting fellow – [remarks](#) on current state, initial implementation observations, and comparability of CAMs
- Nipa Patel, professional accounting fellow – [remarks](#) on audit standard-setting including the SEC's oversight responsibilities, PCAOB standard-setting, and international audit standard-setting

### Corp Fin perspectives at the AICPA conference

In a panel presentation on Corp Fin priorities and observations, Kyle Moffatt, Corp Fin chief accountant, remarked Corp Fin staff is focused on the implementation of CAMs and is reviewing CAMs for consistency with information disclosed elsewhere in the filing (for example, management's discussion and analysis [MD&A], footnotes) with a focus on potential missing disclosures.

Craig Olinger, senior adviser to the chief accountant in Corp Fin, added observations regarding international financial reporting matters including the growing population of foreign private issuers, whether IFRS is appropriate for certain financial statements provided under Rule 3-05 and 3-09 of Regulation S-X, the limited circumstances when the staff will accept qualified opinions, and the appropriate auditing standards to follow for acquired foreign businesses or investees.

## Staff guidance and other initiatives

### Staff updates to existing staff guidance for the adoption of CECL

On Nov. 19, 2019, the SEC issued [SAB 119: "Accounting for Loan Losses by Registrants Engaged in Lending Activities Subject to FASB ASC Topic 326."](#) Presented in a question and answer format, SAB 119 updates existing staff guidance with respect to developing a systematic methodology for estimating credit losses, and it explains the documentation the staff typically would expect registrants to prepare and maintain in support of its estimate of current expected credit losses for lending activities, when material. SABs represent staff interpretations and practices and are not official rules or interpretations of the SEC. SAB 119 is applicable upon a registrant's adoption of Topic 326, and nothing in the SAB should be read to accelerate or delay the effective dates of the standard as modified by the FASB.

### **Omnibus statement on LIBOR transition and potential risks**

On July 12, 2019, SEC staff from multiple divisions and offices published a statement on LIBOR transition that encourages market participants to proactively manage their transition away from LIBOR. The statement identifies several areas that warrant increased attention during the transition period and provides guidance on certain items. Areas addressed in the statement include:

- Identification of existing contracts that extend past 2021 to determine an entity's exposure to LIBOR
- Consideration of whether future contracts should reference an alternative rate to LIBOR or include effective fallback language
- Guidance for how registrants might respond to other business risks associated with the discontinuation of LIBOR such as those related to strategy, products, processes, and information systems
- Questions to consider that will assist an entity in understanding and mitigating the risks related to LIBOR transition
- Potential alternative reference rates
- Guidance from several SEC divisions on responding to risks from the impact of LIBOR discontinuation

It is expected that parties reporting information used to set LIBOR will stop doing so after 2021.

The SEC staff warns, "For many market participants, waiting until all open questions have been answered to begin this important work likely could prove to be too late to accomplish the challenging task required." Chair Clayton also remarked at the AICPA conference that "[h]ope is not a strategy" with respect to LIBOR transition.

### **Corp Fin disclosure review program**

On Sept. 27, 2019, Corp Fin announced the realignment of its disclosure review program. The new structure is aimed at fostering collaboration, transparency, and efficiency. Under the new disclosure review program structure, efforts of Corp Fin staff will be arranged in the following groups:

- **Disclosure Review Program.** This group will conduct the majority of its selective and required filing reviews in seven industry-focused offices.
- **Specialized Policy and Disclosure.** The work of the offices of International Corporate Finance, Mergers and Acquisitions, and Structured Finance as well as corporate governance policy matters across Corp Fin will be included in this group.
- **Office of Risk and Strategy.** This office will provide filing review teams with guidance on developing risks and evolving disclosures.
- **Office of Assessment and Continuous Improvement.** This new office has been established to evaluate the effectiveness of the disclosure review program.

### **Guidance on confidential treatment applications**

On Dec. 19, 2019, Corp Fin staff issued CF Disclosure Guidance: Topic No. 7, "Confidential Treatment Applications Submitted Pursuant to Rules 406 and 24b-2." This guidance addresses how and what to submit when filing an application objecting to public release of information otherwise required to be filed under the *Securities Act* and the *Securities Exchange Act*. This guidance replaces and supersedes the guidance provided in Staff Legal Bulletins 1 and 1A.

## Update to Financial Reporting Manual

Corp Fin published an updated [Financial Reporting Manual](#) on July 1, 2019. The manual provides informal internal guidance from the Corp Fin staff on various accounting topics, financial reporting topics, and SEC rules.

The updated sections are marked “Last updated: 7/1/2019.” Among them:

- Section 1610. Certain guidance on the effect of adopting new accounting standards on selected financial data is removed.
- Topic 2, 2020.1. Application of Rule 3-13 and Note 5 to Rule 8-01 of Regulation S-X is clarified.
- Sections 2030.1, 2030.3. Guidance has been removed. Requests to omit financial statements should be submitted through the Rule 3-13 waiver process.
- Section 5240. Information is consolidated with the note to Topic 2.
- Section 10110. Revenue threshold for emerging growth companies (EGCs) is updated pursuant to SEC Release 33-10332.

## Compliance and Disclosure Interpretation updates

Corp Fin periodically updates its Compliance and Disclosure Interpretations (C&DI). Recent updates include:

- On Feb. 6, 2019 – [Regulation S-K C&DI](#): Questions 116.11 and 133.13 provide guidance on preparing Item 401 disclosure relating to director qualifications and disclosure of self-identified diversity characteristics.
- On Aug. 20, 2019 – [Interactive Data C&DI](#): Questions 101.01 to 101.09 provide guidance on inline eXtensible Business Reporting Language (XBRL) data.
- On Jan. 24, 2020 – [Regulation S-K C&DI](#): Questions 110.02 to 110.04 address omitting a discussion of the earliest of three years from the entity’s current MD&A.

## Capital formation and investor protection

### Corp Fin panel remarks at the AICPA conference

Kyle Moffatt (division chief accountant), Patrick Gilmore (deputy chief accountant), Lindsay McCord (deputy chief accountant), and Craig Olinger (senior adviser to the chief accountant) provided remarks on the practice issues Corp Fin has addressed in the past year including:

- Observations on Rule 3-13 (that is, waiver requests), including the staff’s focus on investor protection and not front-running rule proposals (for example, waiver requests asking to early adopt provisions of the rule proposal regarding disclosures of acquisitions and dispositions of businesses)
- A definitive statement indicating the staff does not plan to revisit the definition of a business in Article 11 of Regulation S-X
- Non-GAAP measures and individually tailored accounting principles (ITAP). Examples of ITAP to which the staff might object include:
  - Measures changing revenue recognition as a principal to revenue recognition as an agent (or vice versa)
  - Contribution margin not reconciled to gross margin presented in accordance with GAAP, which is the most directly comparable GAAP measure
  - Performance measures excluding the impact of the adoption of the credit losses standard or measures that fully exclude an entity’s provision for loan losses
- MD&A, including liquidity disclosures related to supplier finance arrangements
- Predecessor financial statements in initial public offering filings
- Various practice issues related to special purpose acquisition company filings
- The impact of the FASB’s approach to required adoption dates for various standards on:
  - SEC filers that are not smaller reporting companies versus SEC filers that are SRCs in initial registration statements
  - EGCs in the period the entity loses its EGC status



## Rule proposals

### Rulemaking forecast

Chair Clayton and Corp Fin Director Hinman each remarked at the AICPA conference on the staff's efforts to accurately forecast the commission's rulemaking agenda in the near term. The staff's most recent forecast for next action on the following rule proposals appears [online](#).

### Proposal to expand exemption from auditor attestation on ICFR

On May 9, 2019, the SEC issued a proposal, "[Amendments to the Accelerated Filer and Large Accelerated Filer Definitions](#)," which would result in fewer registrants being required to obtain an auditor attestation on the effectiveness of ICFR.

The proposal generally does not change the public float thresholds used to determine filing status. Rather, it adds a revenue test for certain registrants, aimed at scoping out lower-revenue entities that are not large accelerated filers. Specifically, the SEC proposes to exempt SRCs with less than \$100 million in revenue from the requirements of Section 404(b) of the *Sarbanes-Oxley Act of 2002*. The proposal has no impact on the statutory exemption from Section 404(b) afforded to issuers that qualify as an EGC.

The proposal does not change the requirement that companies establish, maintain, and provide management's assessment on the effectiveness of ICFR. The table summarizes the proposed new definitions:

Proposed thresholds and resulting filing status		
Public float	Annual revenues	Filing status
Less than \$75 million	N/A	SRC and nonaccelerated filer (ICFR attestation not required)
\$75 million to \$700 million*	Less than \$100 million*	
\$75 million to \$250 million	\$100 million or more	SRC and accelerated filer
\$250 million to \$700 million	\$100 million or more	Accelerated filer (not SRC)
\$700 million or more	N/A	Large accelerated filer

\*Represents a proposed change to ICFR attestation requirements for issuers with public float between \$75 million and \$700 million and revenues of less than \$100 million.

The proposal also revises certain thresholds, combined with the revenue test, with respect to exiting different tiers of filer status (that is, nonaccelerated, accelerated, or large accelerated filer).

Comments were due July 29, 2019. The staff's most recent forecast for a final rule is April 2020.

### **Proposal for changes to disclosures for business acquisitions and dispositions**

On May 3, 2019, the SEC issued for public comment proposed rule amendments designed to improve information about the acquisition and disposition of businesses. The goal is to facilitate more timely access to capital and to reduce disclosure complexity and compliance costs.

The proposal includes amendments to Rules 3-05 and 3-14, Article 11 of Regulation S-X, and related forms for requirements on information related to financial statements of businesses acquired or to be acquired and for business dispositions. For investment companies, the proposal also includes new Rule 6-11 of Regulation S-X and amendments to Form N-14 for financial reporting of acquisitions involving investment companies.

Proposed changes include, among other things:

- Revising the investment and income significance tests, increasing the use of pro forma financial information in measuring significance, and conforming the significance thresholds and tests for a disposed business
- Requiring acquired business financial statements for a maximum of the two most recent fiscal years instead of three years
- Allowing financial statements that leave out certain expenses for certain acquisitions of a component of an entity
- Clarifying when financial statements and pro forma financial information are required
- Removing the requirement for separate acquired business financial statements once the business has been included in the registrant's post-acquisition financial statements for a whole fiscal year
- Clarifying Rule 3-14 requirements related to determination of significance, the need for interim income statements, special provisions for blind pool offerings, and the scope of the requirements
- Amending the pro forma financial information requirements and disclosures to improve their content and relevance

Comments were due July 29, 2019. The staff's most recent forecast for a final rule is September 2020.

### **Proposal to revise statistical disclosures for banking registrants**

On Sept. 17, 2019, the SEC issued a proposed rule, "Update of Statistical Disclosures for Bank and Savings and Loan Registrants," to modernize statistical disclosures of banking registrants currently provided under Industry Guide 3, "Statistical Disclosure by Bank Holding Companies." The proposal clarifies the types of entities within its scope and carries over, updates, or eliminates various current Guide 3 disclosures. In addition, the proposal rescinds Guide 3 and relocates required disclosures to new Subpart 1400 of Regulation S-K.

The proposal clarifies, for both domestic and foreign registrants, that banks and savings and loan registrants are subject to Subpart 1400 and, with minor exceptions (for example, credit ratio disclosures), matches the periods required for statistical disclosures to the annual and interim periods presented in the financial statements. The proposal carries over many current Guide 3 disclosures to Subpart 1400; however, it also eliminates certain Guide 3 disclosure topics (for example, return on equity and assets and short-term borrowings) and makes minor changes to Article 9 of Regulation S-X.

Significant proposed disclosure changes include increased disaggregation of credit ratios and the addition of certain disaggregated uninsured deposit disclosures.

Comments were due Dec. 2, 2019.

### **Proposal to amend proxy rules**

On Nov. 5, 2019, the SEC voted to propose amendments to modernize rules governing the process for shareholder proposals to be included in a company's proxy statement. It also voted to propose amendments to rules governing proxy solicitations to increase disclosure quality about material conflicts of interest that proxy voting advice businesses provide to their clients.

The shareholder proposal amendments update the criteria, including ownership requirements, for a shareholder to be eligible to require an entity to include a proposal in its proxy statement. Under the proposed amendments, the \$2,000 minimum ownership threshold is maintained; however, to take advantage of that threshold, shares must have been held for at least three years to prove long-term investment in the company. The proposed amendments also clarify that a single person may not submit multiple proposals at the same shareholder's meeting on behalf of different shareholders. Additionally, the amendments update the support levels that a proposal would need to achieve in its first submission to be eligible for resubmission in the following three years.

The proxy voting advice proposal provides that companies that file definitive proxy materials 25 days or more in advance of the relevant meeting have an opportunity for a period of review and feedback through which companies and other soliciting parties would be able to identify errors in the proxy voting advice. This proposal is aimed at improving accuracy and transparency of information provided by proxy voting advice businesses to investors.

Comments were due Feb. 3, 2020.

### **Proposal to amend MD&A, selected financial data, and supplementary financial information**

On Jan. 30, 2020, the SEC proposed amendments to Items 301, 302, and 303 of Regulation S-K. Among other changes, the amendments would:

- Eliminate Item 301 and 302, which would remove requirements for entities to provide selected financial data (SFD) and unaudited quarterly supplementary financial information (SFI)
- Modernize the MD&A requirements in Item 303 through adding a specific disclosure objective, codifying existing staff guidance related to critical accounting estimates, and replacing line item disclosure requirements for off balance sheet arrangements and tabular disclosure of contractual obligations with a principles-based approach

Comments are due 60 days after publication in the federal register.

### **Interpretive guidance related to key performance indicators**

Concurrent with the proposal to amend MD&A, SFD, and SFI, the SEC issued interpretive guidance on key performance indicators and other metrics disclosed in MD&A (collectively, KPIs). The interpretive advice reminds registrants to consider whether any disclosed KPI is subject to an existing regulatory disclosure framework (for example, GAAP, or for non-GAAP measures, Regulation G or Item 10(e) of Regulation S-K, as applicable). If the KPI does not fall within an existing framework, the interpretive guidance specifies the types of disclosures the SEC would expect with respect to the KPI including:

- A clear definition of the metric and how it is calculated
- A statement indicating the reasons why the metric provides useful information to investors
- A statement indicating how management uses the metric in managing or monitoring the performance of the business

When significant estimates or assumptions underlie a KPI, entities should consider whether disclosure of such items is necessary for the KPI disclosure not to be misleading.

Moreover, when a company changes the calculation or method used to present the KPI period over period, the entity should consider disclosure, when material, of:

- Differences in how the metric is calculated or presented period over period
- Reasons for the changes
- Effects of any such changes on the amounts or other information being disclosed and on amounts or other information previously reported
- Other differences in methodology and results that would reasonably be expected to be relevant to understanding the company's performance or prospects

An entity might also need to recast previously reported metrics to conform to the current presentation, depending on the significance of the changes for comparability and user understanding.

Finally, when KPIs are material (for example, to an investment or voting decision), an entity should consider whether it has effective disclosure controls and procedures over such disclosures.

The interpretive guidance is effective upon publication in the federal register.

### **Proposal to modernize Regulation S-K disclosures**

On Aug. 8, 2019, the SEC proposed amendments to modernize certain disclosures under Regulation S-K. The proposal addresses the description of business (Item 101), legal proceedings (Item 103), and risk factor disclosures (Item 105). The proposed amendments are targeted to “improve these disclosures for investors, and to simplify compliance efforts for registrants. Specifically, the proposed amendments are intended to improve the readability of disclosure documents, as well as discourage repetition and disclosure of information that is not material.”

Among other changes to Items 101, 103, and 105, the proposed amendments include the following:

- Item 101. Clarifying and expanding the principles-based approach; adding disclosure topics such as human capital resources, including any material human capital measures or objectives that management focuses on in managing the business, and emphasizing regulatory compliance by including material government regulations
- Item 103. Specifically stating that required information about material legal proceedings may be provided through hyperlinks or cross-references to legal proceedings disclosure located elsewhere in the document
- Item 105. Requiring a summary disclosure if risk factors exceed 15 pages, changing the required disclosure standard from “most significant” to “material” factors, and requiring risk factors to be organized under relevant headings

Comments were due Oct. 22, 2019.

## Final rules

### SEC “test-the-waters” expansion

The SEC adopted, on Sept. 26, 2019, a final rule expanding “test-the-waters” reform to all issuers. All prospective issuers, not just emerging growth companies, are now permitted to assess market interest in a possible initial public offering or other proposed registered securities offering through discussions with potential qualified investors before the filing of a registration statement. These communications will be exempt from *Securities Act* Section 5 restrictions on written and oral offers prior to or after filing a registration statement. The expansion of the “test-the-waters” reform is designed to give companies more flexibility in determining whether to proceed with a registered offering before incurring the costs of preparing a registration statement.

The rule was effective Dec. 3, 2019.

### Regulation Best Interest

On June 5, 2019, the SEC approved Regulation Best Interest, which clarifies that when making recommendations, a broker-dealer may not put its financial interests ahead of the interests of a retail customer. At the same time, the SEC also approved a final rule on new Form CRS relationship summary and Form ADV amendments as well as two interpretations. The interpretations address investment advisers’ standard of conduct and broker-dealer exclusion.

The SEC indicated, “these actions are designed to enhance and clarify the standards of conduct applicable to broker-dealers and investment advisers, help retail investors better understand and compare the services offered and make an informed choice of the relationship best suited to their needs and circumstances, and foster greater consistency in the level of protections provided by each regime, particularly at the point in time that a recommendation is made.”

Registered broker-dealers must begin complying with Regulation Best Interest and broker-dealers and investment advisers registered with the commission will be required to prepare, deliver to retail investors, and file a relationship summary by June 30, 2020.

### Final rule on the FAST Act mandate to simplify and modernize disclosure

On March 20, 2019, the SEC approved a final rule, “FAST Act Modernization and Simplification of Regulation S-K,” to simplify and modernize disclosure requirements for public companies, investment advisers, and investment companies. The new rule, which stems from the SEC’s mandate under the *Fixing America’s Surface Transportation Act* (FAST Act), is intended to improve the readability and navigability of disclosures in SEC filings and to discourage repetition and disclosure of immaterial information. Except as noted here, the final rule was effective on May 2, 2019.

The final rule includes amendments that reduce administrative and disclosure burden by allowing registrants to:

- Exclude, in most cases, the earliest of three years in MD&A, if the discussion has appeared in a prior filing
- Provide disclosure about a physical property only to the extent that it is material to the registrant
- Omit from exhibits:
  - Confidential information in material contracts and certain other exhibits without submitting a confidential treatment request to the SEC, if the information a) is not material and b) would likely cause competitive harm to the registrant if publicly disclosed (*effective April 2, 2019*)
  - Attachments to material agreements if such attachments do not contain material information or were not otherwise disclosed
  - Any document or part thereof that is incorporated by reference in a filing; instead, the registrant will be required to provide hyperlinks to documents incorporated by reference
  - Material contracts entered into within two years of the applicable registration statement or report, if the registrant is not a newly reporting company

New required revisions to filings include:

- Disclosing on the form cover page the national exchange or principal U.S. market for the registrant's securities, the trading symbol, and the title of each class of securities
- Tagging all cover page data with inline XBRL

The final rule also includes parallel changes to several rules and forms applicable to investment companies and investment advisers, including amendments that require certain investment company filings to include a hyperlink to each exhibit listed in the exhibit index of the filings.

The SEC issued minor technical [corrections](#) to the final rule on Aug. 6, 2019.

## Requests for comment

### Request for comment on changes to private securities offering exemptions

The SEC [issued](#), on June 18, 2019, a [request for public comment](#) on ways to simplify, harmonize, and improve the exempt offering framework. The SEC seeks input on possible changes to exemptions for both companies and investors. The release considers:

- Limitations on investors in certain exempt offerings, or the amount they can invest
- Steps to assist in the transition from one offering to another or to a registered offering
- Expanding an entity's ability to raise capital through pooled investment funds
- Revising exemptions covering the secondary trading of securities initially issued in exempt offerings

Comments were due Sept. 24, 2019.

## SEC staff roundtable on short-termism

As part of its follow-on outreach related to a prior [request for comment](#) on earnings releases and quarterly reports, Corp Fin [hosted](#) a public roundtable on July 18, 2019, to gather information from investors, issuers, and other market participants about the impact of short-termism on capital markets and whether the SEC reporting system and regulations should be modified to address these concerns.

The panel discussion covered:

- “Impact of a Short-Term Focus on Our Capital Markets,” to explore the causes and effects of a short-term focus on capital markets and to identify potential market practices and regulatory changes that could encourage long-term thinking and investment
- “Our Periodic Reporting System’s Role in Fostering a Long-Term Focus,” to discuss the SEC’s periodic reporting system and what specific regulatory changes could foster a longer-term focus in the system

In addition, at the AICPA conference, Corp Fin Director Hinman mentioned the current rulemaking agenda includes considering the roundtable remarks in the context of a potential rulemaking to make quarterly reporting less burdensome.

## Other capital formation messages and activities

### SEC chair on modernizing the SEC’s regulatory framework

On Nov. 14, 2019, Chair Clayton [discussed](#) the SEC’s efforts with respect to rulemaking and stakeholder engagement. He highlighted some of the SEC’s key rulemaking accomplishments during 2019 with a view on what is to come. He also outlined the myriad ways the SEC has sought stakeholder engagement in the regulatory process.

### Office of the Advocate for Small Business Capital Formation

The SEC established the new Office of the Advocate for Small Business Capital Formation to provide a voice to small businesses at the SEC, advocate for small businesses and their investors in Washington, D.C., and assist small-business capital formation. According to Martha Miller, director of the office, this mission will be accomplished by:

- “Working with small businesses to understand their capital formation issues through education and outreach;
- “Helping small businesses resolve issues with the SEC and self-regulatory organizations, including by recommending policy changes; and
- “Analyzing the potential impact of proposed rules and regulations likely to significantly affect small businesses.”

On Dec. 19, 2019, the SEC’s Office of the Advocate for Small Business Capital [issued](#) its 2019 annual report, which discusses a summary of the year’s activities, the office’s purpose, small-business capital business formation issues, and policy recommendations.

## Technology and innovation

### **New chief of the Cyber Unit**

On Dec. 2, 2019, the SEC named Kristina Littman chief of the Division of Enforcement's Cyber Unit. The Cyber Unit focuses on protecting investors and markets from cyberrelated misconduct. Littman joined the SEC's Division of Enforcement in 2010 as a staff attorney. Since then, she has held senior attorney positions in the Market Abuse Unit and the Trial Unit.

### **SEC commissioner on cross-border digital assets regulation**

On July 30, 2019, SEC Commissioner Hester Peirce [spoke](#) at the Singapore University of Social Sciences Convergence Forum: Inclusive Blockchain, Finance, and Emerging Technologies, about opportunities for cross-border cooperation for regulating digital assets. She said that innovation in blockchain and cryptocurrency is challenging us "to think about how better to accommodate innovation in general. Because so much of the activity is taking place outside the United States, we have to think about our regulation with a sensitivity for cross-border considerations, cooperation, and what I call co-learning."

Peirce said that regulators' concerns about the cross-border regulation of digital assets in many ways go along with their concerns about regulating all forms of cross-border market activity, including being able to enforce domestic rules, the inability to impose regulations outside U.S. borders, and whether the regulatory structure meets expectations of investors. Peirce warned that international communication and internationalization of markets does not necessarily lead to the internationalization of regulations. She also encouraged jurisdictions to look to regulators for shared consideration of difficult issues and coordination, but not for regulatory directives.

### **2019 FinTech forum**

On May 31, 2019, the SEC hosted a live public forum focusing on distributed ledger technology and digital assets. The forum, which was organized by the SEC's Strategic Hub for Innovation and Financial Technology (FinHub), was [webcast](#) and is now available for [viewing](#) on the FinHub page. The [agenda](#) identified four panel discussions: capital formation considerations, trading and markets considerations, investment management considerations, and distributed ledger technology innovations.

## Other matters of interest

### **New commissioner**

The SEC [announced](#) that on July 8, 2019, Allison Herren Lee was sworn into office as an SEC commissioner with a term ending June 5, 2022. President Donald Trump nominated Lee, who was unanimously confirmed by the U.S. Senate. Chairman Jay Clayton said that Lee's "expertise in securities law, including from her prior tenure at the Commission, will be invaluable to our efforts to advance the interests of investors and our markets."

Commissioner Lee has more than 20 years of experience practicing securities law and has written, lectured, and taught courses internationally on financial regulation and corporate law. She served previously for more than 10 years in several roles at the SEC, including as counsel to former Commissioner Kara Stein and as senior counsel in the Division of Enforcement's Complex Financial Instruments Unit.



### **New chief accountant**

On July 3, 2019, the SEC announced that it named Sagar Teotia to be chief accountant, after he recently served as acting chief accountant. In the position, Teotia will be the principal adviser on accounting and auditing matters, and he will direct the 45 staff members in the SEC's Office of the Chief Accountant. He also will assist the SEC in its oversight of the FASB and the PCAOB. Prior to this position, Teotia served as deputy chief accountant since 2017.

### **Two new deputy chief accountants**

The SEC announced, on Dec. 3, 2019, that it appointed John Vanosdall and Paul Munter as deputy chief accountants in the Office of the Chief Accountant. Vanosdall will head OCA's accounting group. Most recently, he was a partner at PricewaterhouseCoopers LLP, where he concentrated on a range of technical accounting and mergers and acquisitions matters. Previously, he served as an SEC professional accounting fellow.

Munter will lead the OCA's international matters activities. Munter joins the SEC from the University of Colorado Boulder, where he was a senior instructor of accounting. He is a retired partner from KPMG LLP, where he served as the lead technical partner for the U.S. firm's international accounting and International Financial Reporting Standards areas.

## **From the Office of Compliance Inspections and Examinations**

### **2019 examination priorities for broker-dealers**

On Dec. 20, 2019, the SEC's Office of Compliance Inspections and Examinations (OCIE) revealed its most recent broker-dealer examination priorities. According to the release, examination priorities will emphasize "digital assets, cybersecurity, and matters of importance to retail investors, including fees, expenses, and conflicts of interest" and are categorized as follows:

- Compliance and risk for registrants responsible for critical market infrastructure
- Matters of importance to retail investors, including seniors and those saving for retirement
- Financial Industry Regulatory Authority and Municipal Securities Rulemaking Board oversight and examination
- Digital assets
- Cybersecurity
- Anti-money laundering programs

## **From the Division of Enforcement – annual update**

On Nov. 6, 2019, the SEC's Division of Enforcement released its annual update in which the co-directors qualitatively evaluate the performance of the division against five priorities:

- Focus on the Main Street investor
- Focus on individual accountability
- Keep pace with technological change
- Impose remedies that most effectively further enforcement goals
- Constantly assess the allocation of resources

In addition, the annual report provides discussion and analysis of enforcement actions on a quantitative basis.

## From the PCAOB

### Strategic plan and PCAOB leadership priorities

#### Strategic plan

##### PCAOB 2020 budget and five-year strategic plan

On Nov. 19, 2019, the PCAOB approved its fiscal 2020 budget and its five-year strategic plan through 2023. The strategic plan guides the PCAOB's programs, operations, and budget.

The plan includes the following goals:

- “Drive improvement in the quality of audit services through a combination of prevention, detection, deterrence, and remediation.”
- “Anticipate and respond to the changing environment, including emerging technologies and related risks and opportunities.”
- “Enhance transparency and accessibility through proactive stakeholder engagement.”
- “Pursue operational excellence through efficient and effective use of our resources, information, and technology.”
- “Develop, empower, and reward our people to achieve our shared goals.”

#### PCAOB leadership priorities

##### PCAOB at the AICPA conference

The PCAOB provided its perspectives at the conference in three separate sessions:

1. The five members of the board engaged in a panel discussion, which included remarks on:
  - The board's focus on engagement with issuer audit committees
  - Views on the importance of audit quality
  - Changes to the PCAOB's inspection program aimed at improving effectiveness and efficiency
  - Revisions to the format of inspection reports to improve readability and understandability
  - Reaffirmation of the board's five-year strategic plan
2. Megan Zietsman, chief auditor, provided an update on:
  - PCAOB standard-setting activities including:
    - The final standards on auditing estimates and using the work of specialists
    - The auditor's reporting model and critical audit matters
    - An upcoming concept release on changes to quality control standards
  - Consideration of audit firm use of technology or automated tools
3. George Botic, director of the Division of Registrations and Inspections, and Mark Adler, acting director of the Division of Enforcement and Investigations, each presented prepared remarks in a joint session. Among other topics, Botic discussed in more detail the effectiveness and efficiency changes planned for the inspection process and the outlook for 2020 inspections. Adler highlighted the PCAOB's significant enforcement cases in 2019 as well as thoughts on enforcement priorities in the next year.

## A deeper dive on PCAOB leadership priorities

### Engagement with audit committees

#### **Audit committee insights**

On Dec. 18, 2019, the PCAOB posted “[Conversations With Audit Committee Chairs: What We Heard & FAQs](#),” which provides insights gathered from conversations with almost 400 audit committee chairs on what chairs wanted to discuss, perspectives on what is working well to enhance audit quality, an overview of the basics of the PCAOB inspection process, and answers to frequently asked questions that arose during the conversations. Specific topics discussed during those conversations included audit quality, quality of the audit engagement teams, relationship and communication with the auditor, new auditing and accounting standards, and technology-driven changes. FAQs that are answered in the document include:

- Does the PCAOB have resources, educational training, or events for audit committee members?
- Does the PCAOB do a cost-benefit analysis of standards?
- What is the PCAOB’s view of audit quality indicators (AQIs), and how does the PCAOB see them used?

The PCAOB’s strategic plan includes a goal of stakeholder engagement, and while the PCAOB did not meet with audit committee chairs of every engagement inspected during 2019, Chairman William Duhnke remarked during the AICPA conference they have a 2020 goal to meet with 100% of audit committee chairs on inspected engagements.

### Audit quality

On Dec. 17, 2019, the PCAOB voted to issue a concept release covering potential updates to the PCAOB’s quality control (QC) standards. The AICPA developed the current QC standards applicable to PCAOB audits. However, those standards existed prior to the PCAOB, and the auditing environment has changed significantly since that time. Allowing for efficiencies for firms complying with both PCAOB and international standards, the concept release is based in part on proposed international quality control standards with certain incremental or alternative requirements specific to auditing under PCAOB standards (for example, U.S. federal securities laws, SEC rules and regulations, specific PCAOB observations). In conjunction with the issuance of the concept release, PCAOB Chairman Duhnke noted, “[a]n effective quality control system within an audit firm can serve to prevent, identify, and remediate audit quality deficiencies...[t]he input we receive from the public through this concept release will play an important role in the Board’s consideration of an approach to revising our quality control standards.”

Comments are due March 16, 2020.

## Standard-setting

### Estimates and using the work of others

The PCAOB adopted a new auditing standard, “[Auditing Accounting Estimates, Including Fair Value Measurements](#),” on Dec. 20, 2018, to replace three existing PCAOB auditing standards on auditing accounting estimates. Changes to the auditing standard address the auditor’s professional skepticism, including potential management bias, and specific direction on auditing fair values of financial instruments that are based on information from third-party pricing sources. Concurrent with the new standard, the PCAOB adopted amendments related to using the work of a company’s employed or engaged specialists and the work of an auditor’s employed or engaged specialists. Subject to approval by the SEC, the new and amended standards are effective for audits of financial statements for fiscal years ending on or after Dec. 15, 2020.

On July 1, 2019, the SEC [approved](#) PCAOB adoption of 1) the new [audit standard](#) to enhance the requirements that apply when auditing accounting estimates, including fair value measurements, and 2) [amendments](#) to the auditing standards to strengthen requirements for auditors using the work of specialists in an audit. The SEC also approved the application of both standards to the audits of emerging growth companies as necessary or appropriate in the public interest, after considering the protection of investors and whether the action will promote efficiency, competition, and capital formation.

On Aug. 22, 2019, the PCAOB staff [released](#) four new guidance documents to assist auditors in implementing the new audit standards. The staff guidance consists of:

- Auditing accounting estimates
- Auditing the fair value of financial instruments
- Supervising or using the work of an auditor’s specialist
- Using the work of a company’s specialist

The PCAOB maintains implementation pages addressing the new [estimates standard](#) and the [amendments on the auditor’s use of the work of specialists](#).

### Auditor’s reporting model

On Oct. 23, 2017, the SEC approved the PCAOB’s new auditing standard, AS 3101, “[The Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion](#),” which previously was [adopted](#) by the PCAOB on June 1, 2017. The final standard retains the pass-fail reporting model, but it will require auditors to provide additional information in their reports for audits conducted in accordance with PCAOB standards.

In the first phase, the auditor’s report will include:

- Disclosure of the auditor’s tenure
- A statement on independence
- Addition of the phrase “whether due to error or fraud” with regards to whether the financial statements are free of material misstatements
- A standardized form that contains the auditor’s opinion in the first section and section titles
- Requirement that the report be addressed to at least the company’s shareholders and board of directors or equivalents

The first phase applies to audit reports issued on financial statements for fiscal years ending on or after Dec. 15, 2017, which first applies to Dec. 31, 2017, annual financial statements for calendar year-end public companies.

In the second phase, the auditor is required to comply with the most significant change to the auditor's report, which is to communicate CAMs arising during the current period audit. A CAM is defined as a matter that has these elements:

- Was communicated or was required to be communicated to the audit committee
- Relates to accounts or disclosures that are material to the financial statements
- Involves especially challenging, subjective, or complex auditor judgment

The communication of each CAM in the auditor's report will include:

- The identification of the CAMs
- A description of the principal considerations that led the auditor to determine that the matter was a CAM
- A description of how the CAM was addressed
- A reference to the relevant financial statements accounts and disclosures

For large accelerated filers, the second phase is effective for fiscal years ending on or after June 30, 2019, which first applies to Dec. 31, 2019, annual financial statements for calendar year-end large accelerated filers. For all other entities, the second phase is effective for fiscal years ending on or after Dec. 15, 2020, which first applies to Dec. 31, 2020, annual financial statements for calendar year-end public companies that are not large accelerated filers.

The standard does not require communication of CAMs for audits of EGCs, broker-dealers, investment companies other than business development companies, and employee stock purchase, savings, and similar plans.

### **Auditor's reporting model resources**

#### **From the PCAOB**

- The PCAOB released, on Dec. 10, 2019, its first "[Critical Audit Matters Spotlight](#)" report, which presents observations from the PCAOB's review of CAMs on 12 large accelerated filers and includes information about the PCAOB's outreach and data analysis activities. According to the publication, the board believes "that sharing our initial observations from the experiences of the first adopters of CAM requirements could help auditors, companies, audit committees, and other stakeholders."
- The PCAOB released, on July 11, 2019, two resource documents, "[Audit Committee Resource: Critical Audit Matters](#)" and "[Investor Resource: Critical Audit Matters](#)," that give audit committees and investors information about the requirement for auditors to communicate CAMs in audit reports.

The audit committee resource informs audit committees about engaging with their auditors on the CAM requirements. It includes an overview and basics of CAMs as well as PCAOB staff responses to frequently asked questions. It also provides questions audit committees might consider asking their auditors.

The investor resource gives investors information about changes to the auditor's report and understanding the auditor's report, includes investor frequently asked questions about CAMs, and covers the implementation of the standard.

- The PCAOB, on May 22, 2019, released "[Implementation of Critical Audit Matters: A Deeper Dive on the Communication of CAMs](#)" to answer frequently asked questions about how to communicate CAMs. This guidance was developed based on discussions with auditors about their experiences conducting dry runs of CAMs with their audit clients, the staff's review of methodologies submitted by 10 U.S. audit firms that collectively audit approximately 85% of large accelerated filers, and other outreach efforts.

- Three [webinars](#) on implementation of new CAM requirements were held on April 25, May 8, and May 15, 2019. They all covered the same material on CAM determination, communication, and documentation requirements as well as other considerations relevant to CAM requirements. The PCAOB has posted a recording of one of the webinars on its [New Auditor's Report implementation page](#), alongside other resources and recently released staff guidance.
- On March 18, 2019, the PCAOB released three staff guidance documents that address implementation of the new CAM requirements. These new requirements, which phase in from June 30, 2019, through Dec. 15, 2020, will require auditors to communicate CAMs in the auditor's report under PCAOB AS 3101, "The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion."

The three staff guidance documents cover the following:

- "[Implementation of Critical Audit Matters: The Basics](#)" provides a high-level overview of the CAM requirements.
- "[Implementation of Critical Audit Matters: Staff Observations From Review of Audit Methodologies](#)" includes observations from the PCAOB's chief auditor's review of audit firm methodologies.
- "[Implementation of Critical Audit Matters: A Deeper Dive on the Determination of CAMs](#)" includes answers to frequently asked questions for determining CAMs.

Although the staff developed these documents primarily to offer insights for auditors, "The Basics" document also may be of interest to preparers, audit committees, and investors.

Additionally, the PCAOB maintains a CAM implementation [webpage](#) addressing implementation of the new auditor's report. The page provides information, available resources, and training opportunities to auditors and other stakeholders, with particular emphasis on how auditors are preparing to identify and communicate CAMs.

#### From the CAQ

- The CAQ hosted a series of topical CAM webcasts in 2019 including:
  - April 1, 2019 – "[The Enhanced Auditor's Report Is Here: Get the Facts on CAMs and More](#)" addresses early lessons learned in the implementation of CAMs requirements, how audit committees and management can prepare, and how information included in CAMs communications may be used by investors.
  - May 8, 2019 – "[Insights for Audit Committees: Implementation of Critical Audit Matters](#)" discusses questions that audit committees should ask regarding the identification and communication of CAMs in the auditor's report.
  - July 15, 2019 – "[Profession in Focus: Critical Audit Matters, Investors, and Investor Relations](#)" highlights the types of CAM questions investor relations professionals should anticipate.
- On Dec. 10, 2018, the CAQ released a publication, "Critical Audit Matters: Lessons Learned, Questions to Consider, and an Illustrative Example," to share early observations from applying the new PCAOB guidance related to CAMs. Included in the publication are lessons learned from the dry runs of applying the CAMs guidance related to:
  - The determination of which matters are CAMs
  - Auditor communication with management and the audit committee
  - Planning and timing of implementation
  - Challenges in drafting CAMs

Also included in the publication are 10 questions for audit committees to consider related to including CAMs in the auditors' report as well as an illustrative example of a CAM disclosure.

## Inspections

### **Auditor “Inspections Outlook for 2019”**

On Dec. 6, 2018, the PCAOB posted the “Inspections Outlook for 2019” to its website. The report includes key areas of focus for planned 2019 inspections of audits of issuers and brokers and dealers. It covers the following topics:

- System of quality control
- Independence
- Recurring inspection deficiencies
- External considerations
- Cybersecurity risks
- Software audit tools
- Digital assets
- Audit quality indicators
- Changes in the auditor’s report
- Implementation of new accounting standards

Inspections Director Botic mentioned at the AICPA conference the PCAOB will publish a 2020 inspection outlook document.

### **“2019 Staff Inspections Outlook for Audit Committees”**

On March 9, 2019, the PCAOB posted the “2019 Staff Inspections Outlook for Audit Committees” to its website. The document describes the PCAOB’s plans to communicate with audit committees about their core activities, the key areas of focus for the 2019 inspections, and other important topics for audit committees to address with their auditors during the audit. The key areas of focus for planned 2019 inspections include:

- Technological developments
- Audit firms’ actions addressing past inspection findings
- Audit procedures on new accounting standards
- Audit firms’ use of AQIs
- Implementation of new auditor’s reporting model requirements
- Audit firms’ systems of quality control
- Auditor independence

### **Annual broker-dealer inspection report**

On Aug. 20, 2019, the PCAOB released its annual report on 2018 inspections of broker-dealer auditors. The report includes observations from inspections during 2018, insights into applicable standards, and examples of effective procedures. The report highlights that the percentage of deficiencies for audit and attestation engagements remained high and that continued improvement is needed. The PCAOB believes that auditors could achieve significant positive impact on audit quality if auditors:

- Focus on improving their systems of quality control
- Advance their knowledge and understanding of PCAOB standards
- Focus on improving their performance in testing internal controls when employing controls-reliance audit strategies and for examination engagements

The PCAOB also noted that this report will assist broker-dealer owners and audit committees or equivalents when overseeing the work of their auditors.



## Use of technology

### **Cybersecurity, resiliency, and financial regulators' role**

In addition to Chief Auditor Zietsman's comments at the AICPA conference, which included observations on the PCAOB's efforts to analyze the use of technology and data under current auditing standards (for example, AS 2110 and AS 1105), on Oct. 3, 2019, PCAOB board member Kathleen M. Hamm spoke about cybersecurity, resiliency, and the role of financial regulators at the Program on International Financial Systems Technology and Capital Market Regulation Conference in Tokyo, Japan. In her speech, she addressed the nature of cyberthreats, how internet interconnectedness brings significant risks, how financial regulators can address cyberthreats, and the tools available to regulators to defend against cyberthreats. She said, "effective cybersecurity and resiliency includes three key elements: (1) identifying and implementing baseline protections and best practices, (2) engaging in information sharing, and (3) preparing an effective response and recovery plan."

## Other matters of interest

### **Current auditing matters panel discussion**

On June 6, 2019, at the 38th annual SEC and Financial Reporting Institute Conference, a group of industry professionals, including SEC Deputy Chief Accountant Marc Panucci and PCAOB Director Botic, addressed current auditing matters as part of a panel discussion including the following topics:

- Critical audit matters. The panel discussed the importance of identifying tailored CAMs that are specific to the client and based on consideration of both risk assessment and the amount of auditor effort. One panelist shared how his entity's involvement in its audit firm's CAMs pilot resulted in rich, interactive dialogue among the auditors, management, and the audit committee.
- The new standard related to auditing estimates and the use of specialists. The panel noted that the new standard emphasizes increased professional skepticism, model validation, data completeness and accuracy, and specific requirements over the supervision of specialists.
- The new PCAOB inspection process expected to roll out within the year. Botic stressed that the new process is centered on prevention and that some of the changes include audit committee chair interviews for all engagements inspected and the identification of good practices during the inspection process, including audit approaches and testing that lead to high audit quality.



## From the Center for Audit Quality (CAQ)

### 2019 “Audit Committee Transparency Barometer” report

The CAQ and Audit Analytics issued, on Nov. 6, 2019, the 2019 issue of the “Audit Committee Transparency Barometer,” which tracks S&P Composite 1500 proxy disclosures to evaluate transparency regarding audit committee oversight of the external auditor and other important financial reporting topics.

This edition reports that although there has been steady growth in the amount of information provided in audit committee disclosures, there are still significant opportunities to increase transparency. The most growth occurred in the disclosure areas of cybersecurity risk oversight, nonaudit services, and auditor tenure considerations. Audit committees can improve transparency in areas of discussion between the audit committee and external auditor, auditor evaluation, and engagement partner selection and compensation.

The publication also provides disclosure examples.

### Emerging technologies tool for audit committees

On May 16, 2019, the CAQ issued “[Emerging Technologies, Risk, and the Auditor’s Focus: A Resource for Auditors, Audit Committees and Management.](#)” The tool explores financial reporting implications of the evolving use of technology such as artificial intelligence, the internet of things, and smart contracts. Building on the CAQ’s December 2018 publication, “[Emerging Technologies: An Oversight Tool for Audit Committees.](#)” the 2019 tool identifies key risks and provides auditor considerations regarding those risks. It also explores auditor consideration of the impact of emerging technology on business, internal control over financial reporting, and audit committee oversight.

### CECL tool for audit committees

On May 7, 2019, the CAQ released “[Preparing for the New Credit Losses Standard: A Tool for Audit Committees.](#)” This tool is designed to assist audit committees with their oversight responsibilities in implementing the CECL model under Accounting Standards Update 2016-13, “Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.”

The tool has four sections:

1. “Understanding the Standard,” which provides an overview of the standard
2. “Evaluating the Company’s Impact Assessment,” which offers questions for audit committees to consider when discussing the standard’s impact with management and auditors
3. “Evaluating the Implementation Plan,” designed to help audit committees understand and evaluate management’s implementation plan
4. “Other Important Implementation Considerations,” which covers matters such as transition methods and new disclosure requirements

The tool also includes a list of resources produced by leading auditing firms.

## External auditor assessment tool

On April 2, 2019, the CAQ issued an updated tool to assist audit committees in evaluating the external auditor. Focused on audit committees serving public companies, [“External Auditor Assessment Tool: A Reference for U.S. Audit Committees”](#) updates the CAQ’s 2017 publication.

The updated tool adds questions related to firm-level audit quality considerations, including leadership, culture, engagement team management, audit engagement performance, and monitoring. It also includes information about accounting and auditing developments and potential risks. The tool offers questions for audit committees to consider asking in four categories:

- Quality of services and sufficiency of resources provided by the engagement team
- Quality of services and sufficiency of resources provided by the audit firm
- Communication and interaction with the external auditor
- Auditor independence, objectivity, and professional skepticism

The tool suggests audit committees refer to the CAQ’s January 2019 publication [“Audit Quality Disclosure Framework”](#) for additional considerations when asking external auditors about the quality and sufficiency of resources provided by the audit firm.

## Audit quality reporting framework for audit firms

On Jan. 8, 2019, the CAQ released a framework, [“Audit Quality Disclosure Framework,”](#) to assist audit firms in developing transparency or audit quality reports.

The voluntary framework is flexible and addresses disclosure of quality control at the firm level. Under these principles, the framework provides “points of focus” for six elements of audit quality and examples of firm-level AQIs:

1. Leadership, culture, and firm governance
2. Ethics and independence
3. Acceptance and continuance of clients and engagements
4. Engagement team management
5. Audit engagement performance
6. Monitoring

## Learn more

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