



# CENTER FOR AUDIT QUALITY

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## CAQ Public Policy and Technical Alert

JUNE 2017

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*As part of the Center for Audit Quality's ongoing effort to keep members and stakeholders informed on significant public policy and accounting matters, we are pleased to offer the Public Policy and Technical Alert (PPTA). Each month, the PPTA highlights and examines the regulatory, standard-setting, legislative, and broader financial reporting developments impacting the public company audit profession. Please note that the PPTA is intended as general information and should not be relied upon as being definitive or all-inclusive. The CAQ encourages member firms to refer to the rules, standards, guidance, and other resources in their entirety at the hyperlinks provided below. All entities should carefully evaluate which requirements apply to their respective organizations.*

### **In This Issue:**

- PCAOB adopts new auditor reporting standard
- PCAOB proposes standard on auditing accounting estimates
- PCAOB proposes amendments to standards for an auditor's use of the work of specialists
- PCAOB solicits SAG nominations
- PCAOB publishes Staff Inspection Brief previewing the results of 2016 inspections of auditors of broker-dealers
- PCAOB publishes Staff Inspection Brief detailing scope of 2017 inspections of auditors of broker-dealers
- SEC names Division of Enforcement Co-Directors; Division of Corporation Finance Deputy Director
- SEC Division of Corporation Finance expands popular JOBS Act benefit to all companies
- FASB votes to proceed with final hedging standard
- FASB issues proposed ASUs
- IASB proposes amendments to IAS 16
- CAQ releases Form AP tool for audit committees
- CAQ urges auditor focus on disclosures of upcoming accounting changes
- CAQ posts highlights of March 2017 SEC Regulations Committee meeting
- CAQ issues new 'Profession in Focus' videos
- Anti-Fraud Collaboration hosts free CPE webcast on effective policies and internal control
- Upcoming Events

## PCAOB adopts new auditor reporting standard

The Public Company Accounting Oversight Board (PCAOB) on June 1 adopted the auditing standard, [\*The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion\*](#), that will require the auditor to provide additional and important information about the audit in the auditor's report with the objective of making the report more informative and relevant to investors.

The final standard retains the pass/fail opinion of the existing auditor's report but makes significant changes to the auditor's report, including the following:

- *Communication of Critical Accounting Matters (CAM's)* – matters communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements; and (2) involved especially challenging, subjective, or complex auditor judgment;
- *Additional improvements to the auditor's report* – other improvements to the auditor's report that are primarily intended to clarify the auditor's role and responsibilities related to the audit, provide additional information about the auditor, and make the auditor's report easier to read:
  - Auditor tenure – The auditor's report will include a statement disclosing the year in which the auditor began serving consecutively as the company's auditor;
  - Independence – The auditor's report also will include a statement that the auditor is required to be independent;
  - Enhancements to basic elements – Certain standardized language in the auditor's report has been changed, including adding the phrase, "whether due to error or fraud," when describing the auditor's responsibility under PCAOB standards to obtain reasonable assurance about whether the financial statements are free of material misstatements;
  - Standardized form of the auditor's report – The opinion will appear in the first section of the auditor's report. Section titles have been added to guide the reader; and,
  - Addressees – The auditor's report will be addressed to the company's shareholders and board of directors or equivalents (additional addressees also are permitted).

A [Fact Sheet](#) provides additional details.

Subject to approval by the Securities and Exchange Commission (SEC), the final standard and amendments will take effect as follows:

- All provisions other than those related to CAMs will take effect for audits for fiscal years ending on or after December 15, 2017; and,
- Provisions related to CAMs will take effect for audits for fiscal years ending on or after June 30, 2019, for large accelerated filers; and for fiscal years ending on or after December 15, 2020, for all other companies to which the requirements apply.

Auditors may elect to comply before the effective date, at any point after SEC approval of the final standard, pending SEC consideration.

## PCAOB proposes standard on auditing accounting estimates

On June 1, the PCAOB issued for public comment a proposed standard [Auditing Accounting Estimates, Including Fair Value Estimates](#). The proposed standard would replace three existing auditing standards with the intention of promoting strengthened auditing practices by applying a more uniform, risk-based approach to auditing estimates. Specifically, the proposed standard would:

- Prompt auditors to devote greater attention to addressing potential management bias in accounting estimates, while reinforcing the need for professional skepticism;
- Extend certain key requirements in the existing standard on auditing fair value measurements to all accounting estimates to reflect a uniform approach to substantive testing;
- Focus auditors on estimates with greater risk of material misstatement;
- Provide specific requirements and direction to address certain aspects unique to auditing the fair value of financial instruments, including the use of information from third-party pricing sources; and,
- Make other updates to the requirements for auditing accounting estimates to address particular aspects unique to auditing estimates.

The deadline for submitting comments is August 30, 2017. A [Fact Sheet](#) provides additional details.

## PCAOB proposes amendments to standards for an auditor's use of the work of specialists

Also on June 1, the PCAOB issued for public comment [Proposed Amendments to Auditing Standards for Auditor's Use of the Work of Specialists](#). The proposal would change existing requirements in the PCAOB's standards addressing audit evidence and supervision of the audit engagement related to the work performed by specialists. Specifically:

- For use of the work of a *company's* specialist, the proposal would:
  - (a) supplement current requirements in AS 1105 to address circumstances when the auditor uses the work of a company specialist as audit evidence;
  - (b) align requirements with those in the companion proposal on auditing accounting estimates, including fair value measurements; and,
  - (c) remove from the scope of AS 1210 requirements for using the work of a company's specialist as audit evidence.
- For use of the work of an *auditor's* specialist, the proposal would:
  - (a) enhance the requirements for applying a risk-based supervisory approach to auditor-employed specialists, and extend those requirements to auditor-engaged specialists;
  - (b) add requirements for informing the auditor's specialist of the work to be performed and for reviewing and evaluating that specialist's work;
  - (c) amend the requirements for assessing the knowledge, skill, and ability of an auditor's specialist; and,
  - (d) amend the requirements for assessing the objectivity of an auditor-engaged specialist to describe objectivity as the ability to exercise impartial judgment on all issues encompassed by the specialist's work in the audit.

The deadline for submitting comments is August 30, 2017. A [Fact Sheet](#) provides additional details.

## **PCAOB solicits SAG nominations**

The PCAOB on June 13 [announced](#) that it is accepting nominations for the Standing Advisory Group's (SAG) 2018-2020 term. Nominees should have expertise in accounting, auditing, corporate finance, corporate governance, or investing in public companies. The PCAOB also is seeking nominees with experience in auditing or financial reporting for broker-dealers and smaller public companies. The deadline for submissions is August 12, 2017.

## **PCAOB publishes Staff Inspection Brief previewing the results of 2016 inspections of auditors of broker-dealers**

The PCAOB on June 28 published a [Staff Inspection Brief](#) previewing the results of 2016 inspections of auditors of broker-dealers. The inspection plan was consistent with 2015, except that, in 2016, PCAOB Inspections staff focused on the firms' procedures pursuant to the new auditing standard for related party transactions, Auditing Standard 2410, *Related Parties*, which became effective for audits of financial statements for fiscal years beginning on or after December 15, 2014.

PCAOB inspectors continued to observe impaired auditor independence as auditors were involved in the preparation of the financial statements or accounting records of their audit clients. PCAOB Inspections staff continued to observe deficiencies in financial statement audit areas similar to previous inspection cycles, including revenue recognition, financial statement presentation and disclosures, and the assessment of risks of material misstatement due to fraud. In addition, PCAOB inspectors observed that auditors did not sufficiently assess relationships and transactions with related parties.

In 2016, PCAOB inspectors also observed deficiencies in areas including audit procedures on the supporting schedules that accompanied the financial statements; procedures for the attestation engagements: the examinations of compliance reports and the reviews of exemption reports; and engagement quality reviews.

## **PCAOB publishes Staff Inspection Brief detailing scope of 2017 inspections of auditors of broker-dealers**

The PCAOB on June 29 published a [Staff Inspection Brief](#) detailing scope of 2017 inspections of auditors of broker-dealers. PCAOB Inspections staff is focusing on the following broker-dealer audit areas and attestation procedures in 2017:

- Auditor independence;
- Financial statement audit areas where deficiencies were identified in past inspections, including revenue, the assessment and response to risks of material misstatement due to fraud, financial statement presentation and disclosure, fair value measurements, and related party transactions;
- Audit procedures on the supporting schedules to the financial statements;
- Procedures for the attestation engagements: the examination of compliance reports and the review of exemption reports; and,
- Engagement quality reviews.

**SEC names Division of Enforcement Co-Directors; Division of Corporation Finance Deputy Director**

On June 8, the SEC [announced](#) that Acting Director of the Division of Enforcement Stephanie Avakian and former federal prosecutor Steven Peikin have been named Co-Directors of the Division of Enforcement.

- Avakian was named Acting Director of the Division of Enforcement in December 2016 after serving as Deputy Director of the Division since June 2014. Previously, she was a partner at Wilmer Cutler Pickering Hale and Dorr LLP, where she served as a vice chair of the firm's securities practice and represented financial institutions, public companies, boards, and individuals in a broad range of investigations and other matters before the SEC and other agencies.
- Peikin comes to the SEC from Sullivan & Cromwell, where he was Managing Partner of the firm's Criminal Defense and Investigations Group. His practice focused on white-collar criminal defense, regulatory enforcement, and internal investigations. From 1996 to 2004, Peikin served as an Assistant U.S. Attorney in the Southern District of New York, where he was Chief of the Office's Securities and Commodities Fraud Task Force.

On June 20, the SEC [announced](#) that Robert Evans III had been named Deputy Director in the Division of Corporation Finance. He will join Deputy Director Shelley Parratt as a senior advisor to the division's director, William Hinman. Evans comes to the SEC from Shearman & Sterling LLP, where he was a partner in the firm's capital markets practice. He has experience advising on public and private offerings, securities law compliance, and corporate governance.

**SEC Division of Corporation Finance expands popular JOBS Act benefit to all companies**

On June 29, the SEC [announced](#) that the Division of Corporation Finance will permit all companies to submit draft registration statements relating to initial public offerings (IPOs) for review on a non-public basis. This process will be available for IPOs as well as most offerings made in the first year after a company has entered the public reporting system. It will take effect on July 10, 2017.

Permitting all companies to submit registration statements for non-public review, similar to the benefit used by emerging growth companies (EGCs) under the JOBS Act, will provide companies with more flexibility to plan their offering. This expanded nonpublic review process does not limit the process by which EGCs submit draft registration statements for confidential review. The SEC will continue to process those submissions and filed registration statements in the normal course. The announcement also includes other accommodations regarding content of draft registration statements and staff processing to expedite the processing of draft and filed registration statements. Issuers and their advisors are encouraged to review their transaction timing with the staff assigned to the filing review.

Further details regarding the expanded nonpublic review process can be found in the [full announcement](#) on the Division of Corporation Finance's Announcements website.

## **FASB votes to proceed with final hedging standard**

The Financial Accounting Standards Board (FASB) on June 7 [announced](#) that it will proceed with a new accounting standard expected to improve and simplify accounting rules around hedge accounting. The final Accounting Standards Update (ASU) is expected to be published in August 2017.

Under the new standard, hedge accounting will be refined and expanded for both financial (e.g., interest rate) and commodity risks. The economic results will be presented in a more transparent way, both on the face of the financial statements and in the footnotes, for investors and analysts.

The new standard will take effect for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, for public companies and for fiscal years beginning after December 15, 2019 (and interim periods for fiscal years beginning after December 15, 2020), for private companies. Early adoption will be permitted in any interim period or fiscal years before the effective date of the standard.

## **FASB issues proposed ASUs**

In June, the FASB issued three Proposed ASUs:

- [Proposed ASU, Consolidation \(Topic 810\) – Targeted Improvements to Related Guidance for Variable Interest Entities](#)

Issued on June 22, the proposed ASU is intended to reduce cost and complexity and to improve financial reporting associated with consolidation of variable interest entities (VIEs). Under the proposed amendments, a private company would not have to apply VIE guidance to legal entities under common control if both the parent of the commonly controlled group and the legal entity being evaluated for consolidation are not public business entities. Other provisions in the proposed ASU relate to decision-making fees and VIE related party guidance.

A [FASB in Focus](#) provides an overview of the proposed amendments.

The deadline for submitting comments is September 5, 2017.

- [Proposed ASU, Technical Corrections and Improvements to Topic 995, U.S. Steamship Entities: Elimination of Topic 995](#)

Issued on June 27, the proposed ASU would supersede obsolete guidance in Topic 995 on unrecognized deferred taxes related to certain statutory reserve deposits. If an entity has unrecognized deferred income taxes related to statutory deposits made on or before December 15, 1992, the entity would be required to recognize the unrecognized income taxes in accordance with Topic 740.

The deadline for submitting comments is August 28, 2017.

- [Proposed ASU, Technical Corrections and Improvements to Topic 942, Financial Services – Depository and Lending: Elimination of Certain Guidance for Bad Debt Reserves of Savings and Loans](#)

Issued on June 27, the proposed ASU would supersede outdated deferred tax guidance on bad debt reserves of savings and loans that arose after December 31, 1987. The proposed amendments also would supersede guidance related to the Comptroller of the Currency's Banking Circular 202, *Accounting for Net Deferred Tax Charges*.

The deadline for submitting comments is August 28, 2017.

## International

### IASB proposes amendments to IAS 16

The International Accounting Standards Board (IASB) on June 20 [proposed narrow-scope amendments](#) to IAS 16, *Property, Plant and Equipment*, to reduce the diversity in application of the standard. The proposed amendments would prohibit deducting sales proceeds from the cost of an item of property, plant, and equipment while that asset is being made available for use. Instead, the company would recognize those sales proceeds and related costs in profit or loss. The deadline for submitting comments is October 19, 2017.

## CAQ Updates

### CAQ releases Form AP tool for audit committees

The Center for Audit Quality (CAQ) on June 20 published a new tool to aid audit committee members in their understanding of the PCAOB's Rule 3211, *Auditor Reporting of Certain Audit Participants*, which requires registered public accounting firms to file Form AP, with specific disclosures, with the PCAOB for each audit report issued.

The CAQ's publication, [Form AP – Auditor Reporting of Certain Audit Participants: A Tool for Audit Committees](#), is intended to: (1) assist audit committees in discussing the role of audit participants with their engagement partner and company management; and (2) help prepare audit committee members to anticipate potential questions that may arise as a result of these new disclosures. To those ends, the tool provides a summary of Form AP disclosure requirements, as well as suggested questions regarding disclosure of the engagement partner and participation of other accounting firms.

### CAQ urges auditor focus on disclosures of upcoming accounting changes

A June 28 CAQ Alert encourages CAQ members to focus on evaluating the adequacy of management's disclosure of impending changes in accounting principles. The Alert, [SAB Topic 11.M – A Focus on Disclosures for New Accounting Standards](#), addresses requirements that registrants discuss, in their interim and annual SEC filings, the potential effects of recently issued accounting standards when adopted in a future period.

“The new revenue recognition, leases, and credit losses accounting standards become effective over the next few years, and these new accounting standards are expected to present significant changes for many companies,” the Alert says. “Even in situations where a new accounting standard is not expected to significantly impact a registrant's primary financial statements,” the Alert adds, “the accounting standard's requirements related to footnote disclosures may still be a significant change.”

## CAQ posts highlights of March 2017 SEC Regulations Committee meeting

The CAQ posted [highlights](#) from the March 23, 2017 meeting of the SEC Regulations Committee with SEC staff. Among the topics discussed were:

- SAB 74 Disclosures about Newly-Issued Standards;
- Non-GAAP Financial Measures;
- Definition of a Business – Interaction between the new GAAP definition of a business and the S-X Article 11 definition;
- The effects of accounting changes by a successor entity on the predecessor period financial statements;
- Adoption of ASC 606, *Revenue from Contracts with Customers*, when an Emerging Growth Company (EGC) that elected private company adoption dates ceases to qualify as an EGC; and
- Electronic Submission of Pre-Filing Correspondence.

## CAQ issues new 'Profession in Focus' videos

The CAQ issued two new episodes of its online video series, *Profession in Focus*:

- [Episode 46](#) features Douglas R. Carmichael, the Claire and Eli Mason Professor of Accountancy at Baruch College's Zicklin School of Business. Carmichael discusses the benefits of the Sarbanes-Oxley Act, the impact of technology on fraud deterrence, and why professional skepticism is so important.
- [Episode 47](#) features Zoe-Vonna Palmrose, Professor of Accounting and the Kermit O. Hanson Professor in Business Administration at the University of Washington's Foster School of Business. Palmrose, a member of the CAQ's Research Advisory Board, discusses the benefits of internal control over financial reporting, the importance of evidence-based rulemaking, and why, "more than ever, it's important that auditors continue to grow and learn."

## Anti-Fraud Collaboration hosts free CPE webcast on effective policies and internal control

On July 11, the [Anti-Fraud Collaboration](#) will host a free webcast *What Is Your Role? When Accounting Policy Meets ICFR*. The webcast will address the importance of creating accounting policies and effective controls around highly subjective and complex accounting areas that can be easily understood by non-accountants. The expert panel will highlight leading practices that the Collaboration identified through roundtable discussions. All members of the financial reporting supply chain have an important role to play.

Participants will gain insights into:

- How different members of the financial reporting supply chain leverage accounting policies and internal controls to stem fraud and reduce the likelihood of financial restatements;
- The benefits of aligning accounting policies to technical accounting guidance; and
- Developing an effective ICFR regime that accounts for complex accounting areas

This program is free of charge and eligible for 1.8 CPE credits and 1 NACD credit. [Registration](#) is required.



The Anti-Fraud Collaboration consists of four organizations representing members of the financial reporting supply chain: external auditors (through the CAQ), company financial management (through Financial Executives International (FEI)), internal auditors (through The Institute of Internal Auditors (IIA)) and audit committees (through National Association of Corporate Directors (NACD)).

## Upcoming Events

### July 11

Anti-Fraud Collaboration Webcast: “What Is Your Role? When Accounting Policy Meets ICFR” ([Link](#))

### July 11-13

International Corporate Governance Network Annual Conference, Kuala Lumpur, Malaysia ([Link](#))

### July 17-21

IASB Board Meeting, London, UK ([Link](#))

### July 18

FASB Roundtable Meeting, Norwalk, CT ([Link](#))

### July 20

PCAOB Forum on Auditing in the Small Business Environment, New York, NY ([Link](#))

### August 5-9

American Accounting Association Annual Meeting, San Diego, CA ([Link](#))

### September 18-22

IAASB Meeting, New York, NY ([Link](#))

### September 24-27

Investment Company Institute Tax and Accounting Conference, San Antonio, TX ([Link](#))

### October 20

PCAOB Forum for Auditors of Broker-Dealers, Las Vegas, NV ([Link](#))

### October 29-November 1

National Association of State Boards of Accountancy Annual Meeting, New York, NY ([Link](#))

### November 6-8

AICPA Oil & Gas Conference, Denver, CO ([Link](#))

### November 13-14

FEI Current Financial Reporting Issues Conference, New York, NY ([Link](#))

### November 29-30

PCAOB Standing Advisory Group Meeting, Washington, DC ([Link](#))

### December 4-6

AICPA Conference on Current SEC and PCAOB Developments, New York, NY ([Link](#))

**December 7**

PCAOB Forum for Auditors of Broker-Dealers, Jersey City, NJ ([Link](#))

**December 11-15**

IAASB Meeting, New York, NY ([Link](#))

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*The Center for Audit Quality is an autonomous, nonpartisan, nonprofit organization dedicated to enhancing investor confidence and public trust in the global capital markets by fostering high-quality public company audits; collaborating with other stakeholders to advance the discussion of critical issues; and advocating policies and standards that promote public company auditors' objectivity, effectiveness and responsiveness to dynamic market conditions. Based in Washington, D.C., the CAQ is affiliated with the American Institute of CPAs. For more information, visit [www.thecaq.org](http://www.thecaq.org).*

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