



CENTER FOR AUDIT QUALITY

Serving Investors, Public Company Auditors & the Markets
Affiliated with the American Institute of CPAs

CAQ Public Policy Monitor

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As part of the Center for Audit Quality's ongoing effort to keep members informed on critical public policy matters with the potential to impact the public company audit profession, we are pleased to offer the Public Policy Monitor. Each month, the CAQ Public Policy Monitor highlights and examines the policies and broader political events shaping the public debate on public company auditing, as well as financial reporting and related regulatory and legislative issues.

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PCAOB

Standard-Setting

PCAOB proposes to strengthen requirements for supervision of other auditors

The Public Company Accounting Oversight Board (PCAOB or Board) on April 12 [proposed amendments](#) (a [fact sheet](#) is also available) to certain existing standards to strengthen the current requirements and impose a more uniform approach to the lead auditor's supervision of other auditors. The Board also proposed a new auditing standard for situations in which the lead auditor divides responsibility for the audit with another firm. The deadline for submitting comments is July 29.

Specifically, the PCAOB proposes amendments to four Auditing Standards (AS) (numbered according to the Board's reorganized standards):

- AS 1201, *Supervision of the Audit Engagement* – to provide additional direction to the lead auditor on how to apply AS 1201's principles-based supervision provisions to supervision of other auditors;
- AS 2101, *Audit Planning* – to incorporate and update requirements of current standard, AS 1205, *Part of the Audit Performed by Other Independent Auditors*, to specify that they be performed by the lead auditor in an audit that involves other auditors;
- AS 1215, *Audit Documentation* – to require that the lead auditor properly document which specific work papers of other auditors the lead auditor has reviewed, but not retained; and
- AS 1220, *Engagement Quality Review* – to require explicitly that the engagement quality reviewer evaluate the engagement partner's determination of a firm's eligibility to serve as lead auditor.

The proposed new standard, AS 1206, *Dividing Responsibility for the Audit with Another Accounting Firm*, would retain, with modifications, many of the requirements of AS 1205, including the requirement that the lead auditor disclose in its audit report which portion of the financial statements was audited by each other auditor. New requirements would include that the lead auditor:

- Obtain a representation from each other auditor that the other auditor is duly licensed to practice under the applicable laws of the relevant country or jurisdiction;
- Determine whether each other auditor that would play a substantial role in the preparation or furnishing of the lead auditor's report is, or is required to be, registered with the PCAOB; and
- Disclose the name of the other auditor in the lead auditor's report.

Proposed AS 1206 would supersede AS 1205.

PCAOB seeks input for first post-implementation review

The PCAOB on April 6 released a [request for public comment](#) from the Center for Economic Analysis (CEA) that will inform the CEA's first post-implementation review of the overall effect of previously adopted PCAOB rules and standards. The request for comment will provide the CEA with information to evaluate [AS 7, Engagement Quality Review](#) (AS 1220 under the PCAOB's reorganized standards).

The CEA is requesting public comment on the overall effect of AS 7, including the following questions:

- Has AS 7 accomplished its intended purpose?
- Do users of financial statements believe that AS 7 has affected the credibility of financial reporting?
- What have been auditors' experiences with implementation of AS 7?
- What have been preparers' and audit committees' experiences with the implementation of AS 7?
- What have been the initial and recurring costs and benefits associated with the implementation of AS 7 from the perspectives of auditors, preparers, audit committee members, investors and other users of financial statements?
- Could AS 7 be refined or improved to better achieve its intended purpose?

The deadline for submitting comments is July 5.

Reports, Briefs and Alerts

Inspections report describes AS 16 implementation and compliance

The PCAOB on April 5 issued a [report](#) on audit firms' and audit engagement teams' implementation of, and compliance with, AS 16, *Communications with Audit Committees* (AS 1301 under the Board's reorganized standards) and other PCAOB rules and standards related to audit committee communications. The report is based on the Board's 2014 and preliminary 2015 inspection results relating to domestic and non-U.S. registered firms.

PCAOB inspectors found that most firms inspected in 2014 had incorporated the requirements of the standard into their audit methodologies, introduced relevant practice aids, and/or provided training to their partners and staff. Preliminary observations from 2015 inspections show similar results.

Inspections staff identified deficiencies in complying with AS 1301 in seven percent of the audits inspected in 2014. Those deficiencies did not by themselves result in an insufficiently supported audit opinion, but nevertheless constituted departures from the standard's requirements and indicated a potential defect in firms' systems of quality control.

The report concludes with the recommendation that “[a]ll registered firms should review this report and consider whether the auditing deficiencies that the Inspections staff have observed could manifest themselves in their practices. If deficiencies in communications with audit committees have been identified, firms should perform root cause analyses and take appropriate corrective action. Firms also need to monitor and evaluate whether their corrective actions adequately address the deficiencies.”

Staff inspection briefs preview 2015 inspection findings

The PCAOB on April 19 published two staff inspection briefs. The first brief, [Preview of Observations from 2015 Inspections of Auditors of Issuers](#), reports preliminarily that the overall number of audit deficiencies identified in 2015 decreased compared to the results from 2014. Some of the contributing factors to the improvements may include changes in areas such as new practice aids and checklists, coaching and support to teams, and monitoring the quality of audit work performed. The most frequent audit deficiencies continue to be in the key areas related to auditing internal control over financial reporting, assessing and responding to risks of material misstatement, and auditing accounting estimates, including fair value measurements.

The second brief, [Preview of Observations from 2015 Inspections of Auditors of Brokers and Dealers](#), reports preliminarily that inspectors identified fewer independence impairments of auditors of brokers and dealers than in prior years. Inspectors did, however, continue to observe situations where auditors were involved in the preparation of the financial statements or accounting records of their audit clients. Inspections staff also continued to observe deficiencies in financial statement audit areas as well as audit procedures on the supplemental schedules for the computations of net capital and the required reserve. In addition, inspection staff noted deficiencies in the procedures performed for attestation engagements related to the examination of compliance reports and the review of exemption reports under newly applicable PCAOB standards. Deficiencies were also observed in the area of engagement quality review.

Staff alert identifies concerns with improper alteration of audit documentation

The PCAOB on April 21 published [Staff Audit Practice Alert No. 14](#), (Alert) *Improper Alteration of Audit Documentation*. The PCAOB staff prepared the Alert to emphasize that improperly altering audit documentation in connection with a PCAOB inspection or investigation violates PCAOB rules requiring cooperation with the Board's oversight activities and can result in disciplinary actions with severe consequences. Improperly altering audit documentation is also inconsistent with an auditor's professional duty to act with integrity and as a gatekeeper in the public securities markets. Evidence identified in connection with certain recent oversight activities has heightened the staff's concern about such misconduct.

Martin Baumann, the PCAOB's Chief Auditor and Director of Professional Standards, [stated](#) that "PCAOB standards provide specific requirements for auditors to follow if they have legitimate reasons for making changes to audit documentation after the audit has been completed. Auditors must follow those requirements for any changes made."

PCAOB posts updated standard-setting agenda

The PCAOB on March 31 posted to its website an [updated standard-setting agenda](#). The agenda indicates that the PCAOB still plans to re-propose a standard on the auditor's reporting model during the April to September period. However, there has been a change in the Board's plans regarding going concern. Whereas in the January 2016 update the Board said it planned to publish a staff consultation paper, the PCAOB now says the staff will "continue its research and outreach activities to seek input on potential approaches to improving the performance and reporting requirements in the existing standard and addressing the changes in the accounting requirements. These activities could result in a staff consultation paper, a staff audit practice alert, or other possible actions."

SEC

SEC seeks public input on modernizing certain Regulation S-K requirements

The Securities and Exchange Commission (SEC) on April 13 issued the Concept Release, [Business and Financial Disclosure Required by Regulation S-K](#) (Concept Release), to seek public comment on modernizing certain business and financial disclosure requirements in Regulation S-K. The Concept Release is part of the Division of Corporation Finance's Disclosure Effectiveness Initiative.

The SEC is interested in input on whether the disclosure requirements continue to elicit the information that investors need for investment and voting decisions and how registrants can most effectively present the information. The SEC also is seeking comment on the costs and benefits of the disclosure requirements for companies and investors.

The Concept Release specifically requests comments on the following areas relating to business and financial disclosure required in periodic reports filed by companies:

- *The SEC's framework for company disclosure, including the basis and nature of the disclosure requirements.* The Concept Release seeks input regarding topics such as principles-based and prescriptive disclosure requirements, the audience for disclosure and compliance and competitive costs.

- *Information for Investment and Voting Decisions.* Questions raised in this area relate to specific line item requirements of Regulation S-K, whether any disclosure requirements should be modified or eliminated and whether any new disclosure requirements should be added. Among the topics addressed are sustainability disclosures, risk factors, industry specific disclosures, scaled reporting requirements and frequency of interim financial reporting.
- *Presentation and Delivery of Important Information.* The Concept Release raises questions regarding various alternative methods of presenting disclosure that could improve readability and investor access to information, such as cross-referencing, incorporation by reference, hyperlinks and company websites.

The deadline for submitting comments is July 21.

Corp Fin updates Compliance and Disclosure Interpretations

The SEC Division of Corporation Finance (Corp Fin) updated the following section of the Compliance and Disclosure Interpretations (C&DIs):

- Regulation AB – [Information for Form ABS-EE Filings](#) – New questions 1-9 relating to the filing of asset-level disclosures on Form ABS-EE. (Updated 4/28/2016)

FASB/IASB

FASB issues guidance on identifying performance obligations and licensing

The Financial Accounting Standards Board (FASB or Board) on April 14 issued [Accounting Standards Update \(ASU\) 2016-10, Revenue From Contracts With Customers \(Topic 606\): Identifying Performance Obligations and Licensing](#). ASU 2016-10 takes effect at the same time as the new revenue recognition standard.

With respect to performance obligations, ASU 2016-10 adds the following guidance to Topic 606:

- An entity is not required to assess whether promised goods or services are performance obligations if they are immaterial in the context of the contract with the customer.
- An entity is permitted, as an accounting policy election, to account for shipping and handling activities that occur after the customer has obtained control of a good as an activity to fulfill the promise to transfer the good rather than as an additional promised service.

Under Topic 606, an entity evaluates whether promised goods and services are distinct to identify performance obligations in a contract. One of the two criteria for determining whether promises to transfer goods or services are distinct is that the promises are separately identifiable. The ASU is designed to assist in the assessment of whether promises are separately identifiable by:

- Emphasizing that an entity determines whether the nature of its promise in the contract is to transfer each of the goods or services, or whether the promise is to transfer a combined item (or items) to which the promised goods and/or services are inputs.
- Revising the related factors and examples to align with the improved articulation of the separately identifiable principle.

With respect to licensing, the ASU clarifies the guidance in Topic 606 on determining whether an entity's promise to grant a license provides a customer with either a right to use the entity's intellectual property (which is satisfied at a point in time) or a right to access the entity's intellectual property (which is satisfied over time). The ASU also clarifies the scope and applicability of implementation guidance on when to recognize revenue for a sales-based or usage-based royalty promised in exchange for a license of intellectual property.

FASB moving forward with final standard on credit losses

The Board on April 27 [voted to proceed](#) with finalizing the proposed ASU, *Financial Instruments – Credit Losses (Subtopic 825-15)*. The Board expects to issue the final standard in June.

The Board also decided to defer the original effective dates by one year. For public companies that meet the definition of an SEC filer, the ASU will be effective for fiscal years (and interim periods within those fiscal years) beginning after December 15, 2019. Other public companies will be required to apply the guidance for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years. Early adoption will be permitted for all organizations for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years.

FASB proposes technical corrections and improvements, amendments to Topic 230

- The FASB on April 21 issued the proposed ASU, [Technical Corrections and Improvements](#). The proposed ASU includes simplification and minor improvements to Topics on insurance and troubled debt restructuring that result in numerous editorial changes to the Accounting Standards Codification. The changes are not expected to affect current accounting practice or result in any significant costs. The deadline for submitting comments is July 5.
- On April 28, the FASB issued the proposed ASU, [Statement of Cash Flows \(Topic 230\): Restricted Cash](#) (a consensus of the FASB Emerging Issues Task Force). The proposed ASU would require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents would be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The deadline for submitting comments is June 27.

IASB issues amendments to revenue standard

The International Accounting Standards Board (IASB) on April 12 [issued amendments](#) to IFRS 15, *Revenue from Contracts with Customers*, clarifying some requirements and providing additional transitional relief for companies that are implementing the new standard. The amendments specifically clarify how to:

- Identify a performance obligation (the promise to transfer a good or a service to a customer) in a contract;
- Determine whether a company is a principal (the provider of a good or service) or an agent (responsible for arranging for the good or service to be provided); and
- Determine whether the revenue from granting a license should be recognized at a point in time or over time.

In addition to the clarifications, the amendments include two additional reliefs to reduce cost and complexity for a company when it first applies the new standard. The amendments have the same January 1, 2018 effective date as IFRS 15.

International

New international research explores audit skills of the future

The Institute of Chartered Accountants of Scotland and the U.K. Financial Reporting Council on April 6 published two international studies on the ideal composition of modern audit teams and how they can best meet future demands:

- The first study, [*Skills, Competencies and the Sustainability of the Modern Audit*](#), found, for example, that: there is a need for a constructive debate about the future of audit; there is an increasing need in audit teams for people with more diverse backgrounds; specialists should be recruited and then trained in audit to become an effective part of the audit team; and there should be more focus on the development of mid-career professionals.
- The second study, [*The Capability and Competency Requirements of Auditors in Today's Complex Global Business Environment*](#), identifies 11 areas of difficulty where the challenges lie for auditors, covering four broad categories: the context of the specific audit engagement; the development of audit personnel; firms as suppliers of audit services; and interactions with stakeholders and society.

IOSCO cybersecurity study reviews regulatory approaches, best practices

The International Organization of Securities Commissions (IOSCO) on April 6 published a [report](#) that brings together insights and perspectives from IOSCO's various policy, stakeholder, and regional committees on the topic of cyber risk.

For securities regulators, the report provides an overview of some of the different regulatory approaches to cybersecurity and the potential tools available to regulators to respond to cyber risk. For market participants, the report outlines various plans and measures participants have put in place to enhance cybersecurity in terms of identification, protection, detection, response and recovery. In doing so, the report describes some of the practices adopted by market participants and aims to encourage, where appropriate, the adoption of those or similar practices.

CAQ Updates

CAQ issues new 'Profession in Focus' video

The Center for Audit Quality (CAQ) issued one new episode of its online video series, *Profession in Focus*:

- In [Episode 21](#), Anne Sheehan, Director of Corporate Governance at the California State Teachers' Retirement System, discusses the importance of board diversity to investors, the desire of investors for a window into the activity of audit committees, and why effective disclosure is not just about reducing the quantity of what's disclosed.

Upcoming Events

May 11

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

May 12

FASB Emerging Issues Task Force Educational Meeting, Norwalk, CT ([Link](#))

May 16

FEE/CCAB/CFA Institute Roundtable: The Future of Corporate Reporting, London, UK ([Link](#))

May 17-19

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

May 18-19

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

May 20

IFRS Foundation Conference, “Implementing the IFRS 16 Leases Requirements,” London, UK ([Link](#))

May 23-24

FEI Financial Leadership Summit Conference, Colorado Springs, CO ([Link](#))

May 24-26

IFRS Foundation Trustees Meeting, Jakarta, Indonesia ([Link](#))

June 1

PCAOB Forum for Auditors of Broker-Dealers, Chicago, IL ([Link](#))

June 2

PCAOB Forum on Auditing in the Small Business Environment, Chicago, IL ([Link](#))

June 7

SEC/FINRA Compliance Outreach Regional Seminar, Dallas, TX ([Link](#))

June 12-17

ACFE Global Fraud Conference, Las Vegas, NV ([Link](#))

June 14

SEC/FINRA Compliance Outreach Regional Seminar, Boston, MA ([Link](#))

June 21-24

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

June 21

PCAOB Forum on Auditing in the Small Business Environment, Philadelphia, PA ([Link](#))

June 21

PLI Seminar/Webcast: Audit Committees and Financial Reporting 2016: Recent Developments and Current Issues, New York, NY ([Link](#))

June 22-25

Society of Corporate Secretaries & Governance Professionals National Conference, Colorado Springs, CO ([Link](#))

June 27-29

ICGN Annual Conference, San Francisco, CA ([Link](#))

July 17-20

IIA 2016 International Conference, New York, NY ([Link](#))

July 21

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

July 21-22

AICPA National Advanced Accounting and Auditing Technical Symposium, Salt Lake, UT ([Link](#))

July 25

SEC/FINRA Compliance Outreach Regional Seminar, Chicago, IL ([Link](#))

August 6-10

American Accounting Association Annual Meeting, New York, NY ([Link](#))

August 18

SEC/FINRA Compliance Outreach Regional Seminar, San Francisco, CA ([Link](#))

September 21-23

AICPA National Conference on Banks & Savings Institutions, National Harbor, DC ([Link](#))

September 22

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

September 22-23

PLI SEC Reporting & FASB Forum for Mid-sized & Smaller Companies, Las Vegas, NV ([Link](#))

September 28-30

CII 2016 Fall Conference, Chicago, IL ([Link](#))

October 16-18

American Bankers Association Annual Convention, Nashville, TN ([Link](#))

October 18

PCAOB Forum for Auditors of Broker-Dealers, Tampa, FL ([Link](#))

October 19

PCAOB Forum on Auditing in the Small Business Environment, Tampa, FL ([Link](#))

October 24-26

AICPA Conference on Credit Unions, Orlando, FL ([Link](#))

October 30-November 2

NASBA Annual Meeting, Austin, TX ([Link](#))

November 13-15

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

November 16-18

AICPA Health Care Industry Conference, Nashville, TN ([Link](#))

November 30-December 1

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

December 5-6

AICPA Employee Benefit Plans Accounting, Auditing and Regulatory Update, Washington, DC ([Link](#))

December 5-7

AICPA Conference on Current SEC and PCAOB Developments, Washington, DC ([Link](#))

December 7

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

December 8

PCAOB Forum on Auditing in the Small Business Environment, Las Vegas, NV ([Link](#))

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.

The CAQ Public Policy Monitor represents the observations of the CAQ, but not necessarily the views of particular member firms, Governing Board members or individuals associated with the CAQ. Questions and comments about the CAQ Public Policy Monitor can be addressed to: ppm@thecaq.org.