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# **CAQ Public Policy and Technical Alert**

JUNE 2016

*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 will highlight and examine 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.*

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## PCAOB

### PCAOB issues staff guidance for firms filing the new Form AP

The Public Company Accounting Oversight Board (PCAOB) on June 28 issued [Staff Guidance – Form AP, Auditor Reporting of Certain Audit Participants and Related Voluntary Audit Report Disclosure Under AS 3101, Reports on Audited Financial Statements](#). The PCAOB in December 2015 adopted new rules requiring that firms disclose engagement partners' names and other firms participating in public company audits on a new Form AP. For public company audit reports issued on or after January 31, 2017, Firms are required to list engagement partner names in Form AP., For public company audit reports issued on or after June 30, 2017, Form AP must also include other audit firms that participated in the audit.

The staff guidance covers provisions of the new rules, such as assigning engagement partner identification numbers and estimating audit hours when disclosing the participation of other accounting firms, among other things.

The PCAOB also launched a [web resource page](#) on Form AP for investors, auditors, and others interested in the information. The web page provides additional resources to audit firms preparing to comply with the new rules, such as general instructions for the Form AP and a sample form that can be downloaded for reference.

## SEC

### SEC adopts amendment to Form 10-K implementing FAST Act provision

The SEC on June 1 approved an [interim final rule](#) to allow Form 10-K filers to provide a summary of business and financial information contained in the annual report. The interim final rule provides filers with flexibility in preparing the summary and those opting to provide it must include hyperlinks to the related, more detailed disclosure in the Form 10-K. It also requests comment on whether the rule should include specific requirements or guidance for the form and content of the summary and whether the rules should be expanded to include other annual reporting forms.

The interim final rule, which implements a provision of the Fixing America's Surface Transportation (FAST) Act, became effective on June 9 and the SEC is accepting public comments through July 11.

### SEC permits voluntary filing using Inline XBRL

The SEC on June 13 [issued an order](#) under the Securities Exchange Act of 1934 to permit, but not require, companies to use Inline eXtensible Business Reporting Language (XBRL) in their periodic and current reports through March 2020. Inline XBRL enables filers to integrate XBRL structured data within their HTML documents rather than as an exhibit to the filings.

According to the order, "Inline XBRL has the potential to provide a number of benefits to filers and users of the information. For example, Inline XBRL could decrease filing preparation costs, improve the quality of structured data, and, by improving data quality, increase the use of XBRL data by investors and other market participants."

## **SEC proposes modernized property disclosures for mining registrants**

The SEC on June 16 [proposed rules](#) to modernize the disclosure requirements for mining properties by aligning them with current industry and global regulatory practices and standards. The proposed revisions would update disclosure requirements for mining registrants in Item 102 of Regulation S-K under the Securities Act of 1933 and the Securities Exchange Act of 1934 and related guidance in Industry Guide 7.

Specifically, the proposed rules would:

- Provide one standard requiring registrants to disclose mining operations that are material to the company's business or financial condition;
- Require a registrant to disclose mineral resources and material exploration results in addition to its mineral reserves;
- Permit disclosure of mineral reserves to be based on a preliminary feasibility study or a final feasibility study;
- Provide updated definitions of mineral reserves and mineral resources;
- Require, in tabular format, summary disclosure for a registrant's mining operations as a whole as well as more detailed disclosure for material individual properties;
- Require that every disclosure of mineral resources, mineral reserves and material exploration results reported in a registrant's filed registration statements and reports be based on, and accurately reflect information and supporting documentation prepared by, a "qualified person;"
- Require a registrant to obtain a technical report summary from the qualified person, which identifies and summarizes for each material property the information reviewed and conclusions reached by the qualified person about the registrant's exploration results, mineral resources or mineral reserves.

The deadline for submitting comments is August 26.

## **CorpFin updates C&DIs**

On June 23, the SEC's Division of Corporation Finance (CorpFin) updated the following section of the Compliance and Disclosure Interpretations (C&DIs):

- Securities Act Rules – [New questions 271.17-271.23](#) – Application of Rule 701 in the context of merger transactions.

## **SEC proposes amendments to smaller reporting company definition**

On June 27, the SEC [proposed amendments](#) to its definition of "smaller reporting company" (SRC) to enable a company with less than \$250 million of public float to provide scaled disclosures as an SRC, as compared to the \$75 million threshold under the current definition. In addition, a company with no public float would be permitted to provide scaled disclosures if its annual revenues were less than \$100 million, as compared to the current threshold of less than \$50 million in annual revenues. As in the current rules, once a company exceeds either of the thresholds, it will not qualify as an SRC again until public float or revenues decrease below a lower threshold. Under the proposal, a company would qualify only if its public float is less than \$200 million or, if it has no public float, its annual revenues are less than \$80 million.

The SEC is not proposing to increase the \$75 million threshold in the "accelerated filer" definition. Companies with \$75 million or more of public float that would qualify as SRCs under the proposed amendments would remain subject to the requirements that currently apply to accelerated filers, including

the timing of the filing of periodic reports and the requirement that accelerated filers provide the auditor's attestation of management's assessment of internal controls over financial reporting (ICFR) required by Section 404(b) of the Sarbanes-Oxley Act (SOX).

The deadline for submitting comments is August 30, 2016.

## **SEC adopts disclosure rules for resource extraction issuers**

The SEC on June 27 adopted [final rules](#) to require resource extraction issuers to disclose payments made to governments for the commercial development of oil, natural gas or minerals. The rules were mandated by the Dodd-Frank Act.

The final rules require an issuer to disclose payments made to the U.S. federal government or a foreign government if the issuer engages in the commercial development of oil, natural gas, or minerals and is required to file annual reports with the SEC under the Securities Exchange Act. The issuer must also disclose payments made by a subsidiary or entity controlled by the issuer. Under the final rules, resource extraction issuers must disclose payments that are: made to further the commercial development of oil, natural gas, or minerals; "not de minimis" (defined as any payment, whether a single payment or a series of related payments, which equals or exceeds \$100,000 during the same fiscal year); and within the types of payments specified in the rules. The final rules define commercial development of oil, natural gas, or minerals as exploration, extraction, processing, and export, or the acquisition of a license for any such activity. The [Press Release](#) announcing the final rule contains an overview of the rule's provisions.

Resource extraction issuers are required to comply with the rules starting with their fiscal year ending no earlier than September 30, 2018.

## **SEC names new Senior Adviser to the Chair for Cybersecurity Policy**

The SEC on June 2 announced the appointment of [Christopher Hetner](#) as Senior Adviser to the Chair for Cybersecurity Policy. In this role, Hetner will be responsible for coordinating efforts across the SEC to address cybersecurity policy, engaging with external stakeholders, and further enhancing the SEC's mechanisms for assessing broad-based market risk. Previously, he was Cybersecurity Lead for the Technology Control Program within the SEC's Office of Compliance Inspections and Examinations.

## **FASB/IASB**

### **FASB releases new, proposed ASUs**

The Financial Accounting Standards Board (FASB) issued one new Accounting Standards Update (ASU) in June:

- [ASU 2016-13](#), *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The ASU's main objective is to provide financial statement users with more useful information about expected credit losses. This objective is achieved by:
  - Removing the probable threshold in current GAAP;
  - Broadening the range of information that is considered in determining expected credit losses; and
  - Providing enhanced disclosures.

*Effective date:* For public business entities that are SEC filers, the ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. For all other public business entities, the ASU effective for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years. For all other entities, the ASU is effective for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. Early adoption is available for all entities as of the fiscal years beginning after December 15, 2018, including interim periods within those fiscal years.

To assist financial statement users with the transition to ASU 2016-13, the FASB also released a [4-page summary](#) of the ASU a [summary](#) of how the FASB considered the expected costs and benefits, and a [video](#) entitled *Why a New Credit Losses Standard?*

The FASB also issued two proposed ASUs in June:

- Proposed ASU, [\*Other Income – Gains and Losses from the Derecognition of Nonfinancial Assets \(Subtopic 610-20\): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets\*](#), would clarify the scope of the nonfinancial asset guidance in Subtopic 610-20 to specify that an in substance nonfinancial asset is an asset of the reporting entity included in either of the following:
  - A contract in which substantially all of the fair value of the assets promised to a counterparty is concentrated in nonfinancial assets; or
  - A consolidated subsidiary in which substantially all of the fair value of the assets in the subsidiary is concentrated in nonfinancial assets.

The proposed ASU also would clarify that an in substance nonfinancial asset is neither of the following:

- A group of assets or subsidiary that is a business or nonprofit activity; or
- An investment of a reporting entity (for example, an equity method investment) regardless of whether the assets underlying the investment would be considered in substance nonfinancial assets.

The derecognition of all businesses (including real estate businesses) and nonprofit activities would, as a result of the proposed ASU, be accounted for in accordance with the derecognition and deconsolidation guidance in Subtopic 810-10. In addition, the proposed ASU would eliminate the exception in the financial asset guidance for transfers of investments (including equity method investments) in real estate entities.

The deadline for submitting comments is August 5.

- Proposed ASU, [\*Consolidation \(Topic 810\): Interests Held through Related Parties That Are under Common Control\*](#), would amend the guidance in ASU 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis*, on how a reporting entity that is the single decision maker of a variable interest entity (VIE) would treat indirect interests in the entity held through related parties that are under common control with the reporting entity when determining whether it is the primary beneficiary of that VIE.

The deadline for submitting comments is July 25.

## **IASB issues narrow-scope amendments to IFRS 2; proposes amendments to IFRS 3 and 11**

The International Accounting Standards Board (IASB) on June 20 [issued amendments](#) to IFRS 2, *Share-based Payment*, clarifying how to account for certain types of share-based payment transactions. Specifically, the amendments provide requirements on the accounting for:

- The effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments;
- Share-based payment transactions with a net settlement feature for withholding tax obligations; and
- A modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

Companies are required to apply the amendments for annual periods beginning on or after January 1, 2018. Earlier application is permitted.

On June 28, the IASB [proposed amendments](#) to IFRS 3, *Business Combinations*, and IFRS 11, *Joint Arrangements*, to clarify both the definition of a business and how to account for previously held interests. Specifically, the proposed amendments would clarify:

- The definition of a business; and
- The accounting for previously held interests when an entity obtains control of a business that is a joint operation and when it obtains joint control of a business that is a joint operation.

The deadline for submitting comments is October 31.

## **International**

### **IOSCO issues guidance on non-GAAP financial measures**

The International Organization of Securities Commissions (IOSCO) on June 7 issued the [Statement on Non-GAAP Financial Measures](#) (Statement). The Statement is intended to assist issuers in providing clear and useful disclosure for investors and other users of financial measures other than those prescribed by Generally Accepted Accounting Principles (GAAP), and in reducing the risk that such measures are presented in a way that could be misleading.

“Non-GAAP financial measures can be useful to issuers and investors because they can provide additional insight into an issuer’s financial performance, financial condition and/or cash flow,” the Statement says. “The use of non-GAAP financial measures also can provide issuers with flexibility in communicating useful, entity-specific information. Problems can arise, however, when non-GAAP financial measures are presented inconsistently, defined inadequately, or obscure financial results determined in accordance with GAAP. Furthermore, non-GAAP financial measures typically lack a standardized meaning and, if so, are generally not comparable from one issuer to the next.”

The Statement identifies the following general elements as a framework for the disclosure of non-GAAP financial measures:

- Defining the Non-GAAP Financial Measure;
- Unbiased Purpose;
- Prominence of Presentation of GAAP Measures Versus Non-GAAP Financial Measures;



- Reconciliation to Comparable GAAP Measures;
- Presentation of Non-GAAP Financial Measures Consistently Over Time;
- Recurring Items; and
- Access to Associated Information.

## U.S. Congress

### House legislation seeks PCAOB, SEC reforms

On June 7, House Financial Services Chairman Jeb Hensarling (R-Texas) [outlined legislation](#) he intends to introduce very soon. The *Financial Creating Hope and Opportunity for Investors, Consumers and Entrepreneurs (CHOICE) Act*'s primary aim is to provide financial institutions with relief from the Dodd-Frank Act. But the legislation will also include a number of audit- and financial reporting-related provisions, including to:

- Increase the civil penalties that the PCAOB may impose on a registered public accounting firm from \$2 million to \$2,750,000, and from \$100,000 to \$150,000 for an individual associated with such a firm;
- Amend Section 105(c)(2) of SOX to require the PCAOB to hold its disciplinary proceedings in public, unless the Board, on its own motion or after considering such a motion of a party, orders otherwise;
- Amend Section 104(g) of SOX to ensure that the PCAOB is fully responsive and accountable to Congress;
- Amend Section 109(c) of SOX to require that all fines collected by the PCAOB be remitted to Treasury for deficit reduction;
- Expand the SOX Section 404(b) exemption for non-accelerated filers to include issuers with up to \$250 million in market capitalization (up from the current threshold of \$75 million) or \$1 billion in assets for banks;
- Extend the time period in which emerging growth companies (EGCs) must comply with Section 404(b); and
- Provide a voluntary exemption for all EGCs and other issuers with annual gross revenues under \$250 million from the SEC requirements to file financial statements in XBRL.

On June 23, the Financial Services Committee made available a [discussion draft](#) of the nearly 500-page bill as well as a [section-by-section summary](#). Hensarling, speaking at the Heritage Foundation on the 23<sup>rd</sup>, said his goal is to mark up the *Financial CHOICE Act* in September.

Rep. Scott Garrett (R-N.J.) on June 9 introduced [H.R. 5429](#), the *SEC Regulatory Accountability Act*, to improve the SEC's consideration of the costs and benefits of its regulations and orders. The bill would amend Section 23 of the Securities and Exchange Act of 1934 by requiring that the SEC, before issuing a regulation under the securities laws:

- Clearly identify the nature and source of the problem that the proposed regulation is designed to address, as well as assess the significance of that problem, to enable assessment of whether any new regulation is warranted;
- Utilize the Chief Economist to assess the costs and benefits, both qualitative and quantitative, of the intended regulation and propose or adopt a regulation only on a reasoned determination that the benefits of the intended regulation justify the costs of the regulation;

- Identify and assess available alternatives to the regulation that were considered, including modification of an existing regulation, together with an explanation of why the regulation meets the regulatory objectives more effectively than the alternatives; and
- Ensure that any regulation is accessible, consistent, written in plain language, and easy to understand and shall measure, and seek to improve, the actual results of regulatory requirements.

The bill also includes a resolution expressing Congress' opinion that the PCAOB should comply with these requirements.

The House Financial Services Committee approved the bill on June 16 by a vote of 34 to 25.

## Other Developments

### COSO proposes updates to ERM Framework

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) on June 14 released a [proposed update](#) to its *Enterprise Risk Management – Integrated Framework* and is seeking public comment of the proposal. The comment period closes on September 30.

The proposed update, is designed to address the needs of all organizations to improve their approach to managing new and exist-ing risks as a way to help create, preserve, sustain and realize value. The proposal updates the core definitions of “risk” and “enterprise risk management” as well as the components of enterprise risk management. It also introduces principles that reflect the evolution of risk management thinking and practices.

## CAQ Updates

### CAQ publication highlights composition of audit committees of the future possible audit committee enhancements

The Center for Audit Quality (CAQ) and the John L. Weinberg Center for Corporate Governance at the University of Delaware in April convened an expert panel to explore the composition of the audit committee of the future. In June, the CAQ published [CAQ Insights: The Audit Committee of the Future](#), which summarizes the panelists' views on what skills audit committees will need, especially in light of emerging challenges such as cybersecurity, as well the possibility of the SEC or the stock exchanges reexamining the definition of an “audit committee financial expert” (ACFE). The panelists also considered whether investors are getting enough information about the experience of audit committee members.

The CAQ identified five recurring themes in the discussions regarding what panelists thought would lead to stronger audit committees:

1. *Tightening the ACFE definition (carefully)*: Several on the panel advised against imposing excessive requirements regarding board expertise, warning that flexibility could be lost. However, a few panelists suggested ways the ACFE definition might be tightened by, for example, eliminating the supervisory element of the SEC's ACFE definition, or imposing higher standards for knowledge of GAAP or GAAS.



2. *Enhancing voluntary audit committee disclosure:* Across the board, panelists believed that voluntary disclosure is a critical first step to improving communication around audit committee composition and expertise, particularly given that some audit committees may not be adequately disclosing the expertise they already have.
3. *Fostering robust communication and engagement:* In addition to enhancing communication with investors and other parties via disclosure, panelists agreed that audit committees need to focus strongly on developing healthy channels of internal communication.
4. *Prioritizing continuing education:* Several panelists stressed the importance of continuing education for audit committee members, especially given the growing complexity of accounting standards and financial reporting rules.
5. *Addressing the “kitchen sink” challenge:* While tasked with a critical responsibility – oversight of the company’s financial reporting process – many audit committees have seen workloads expand into areas that may be loosely related. Working to avoid blurring of the committee’s focus can help when thinking through composition.

A [companion video](#) explores the ACFE issue. In addition to providing an overview of the financial expertise requirement for audit committees, the video features commentary on the issue from audit committee members at Freddie Mac, Microsoft, PPG Industries, SanDisk, and Wal-Mart Stores.

### **CAQ tool helps audit committees continue to examine use of non-GAAP measures**

The CAQ on June 28 released a new tool to help audit committees continue to assess management’s presentation, outside the audited financial statements, of performance metrics that do not conform to GAAP. The publication, [Questions on Non-GAAP Measures: A Tool for Audit Committees](#), can assist in the determination of whether non-GAAP indicators provide investors with meaningful financial information.

The publication groups its questions under three core categories:

- *Transparency:* The tool offers audit committees ways to consider the purpose, prominence, and labeling of non-GAAP information, specifically in relation to traditional GAAP measurements;
- *Consistency:* The tool suggests ways that audit committees can question management to determine whether non-GAAP measures are consistent and balanced; and
- *Comparability:* The tool provides questions to promote the comparability of non-GAAP measures presented.

The tool also reviews current regulation governing non-GAAP information, as well the auditor’s role in this area.

### **Highlights of SEC Regulations Committee meeting now available**

The CAQ posted on its website [highlights](#) from the March 21 meeting of the SEC Regulations Committee with SEC staff. Among the topics addressed were:

- Transition Questions Related to New Leasing Standard;
- FAST Act Filing Accommodations;
- Conflict Minerals;
- Financial Reporting Manual (FRM) Updates;
- Disclosure Effectiveness Update;
- Non-GAAP Measures;

- Supplemental Pro Forma MD&A in Connection with New Revenue Recognition Standard (ASC 606); and
- General Instruction II.C of Form S-1 or General Instruction II.E of Form F-1 to Pro-Forma Financial Information

## CAQ issues new 'Profession in Focus' videos

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

- [Episode 24](#) features Brian T. Croteau, Deputy Chief Accountant at the SEC. Among other topics, Croteau discusses the state of audit quality, implementation of new accounting standards, internal control over financial reporting, and his lessons learned in six years of public service.
- [Episode 25](#) features Wayne Berson, the CEO of BDO USA and a member of the CAQ's Governing Board. Berson provides views on talent in the auditing profession, the role of technology, growth of his firm, and the significance of BDO's charitable endeavors.

## CAQ's Fornelli discusses ICFR

At her [LinkedIn Influencer](#) page, CAQ Executive Director Cindy Fornelli discussed the importance of effective ICFR to investor protection and how stakeholders from across the financial reporting supply chain have elevated the debate and dialogue around ICFR to new heights.

## Upcoming Events

### July 17-20

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

### July 18-22

IASB Board Meeting, London, UK ([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 14-15**

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

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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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