



CENTER FOR AUDIT QUALITY

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

CAQ Public Policy and Technical Alert

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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.

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PCAOB

PCAOB staff inspection briefs detail scope and objectives of 2016 inspections

The Public Company Accounting Oversight Board (PCAOB) on July 14 issued two staff inspection briefs: (1) on the [2016 inspections of registered audit firms and their audits of issuers](#), and (2) on the [2016 inspections of auditors of brokers and dealers](#) registered with the Securities and Exchange Commission (SEC).

Public Company Audits. The staff inspection brief for registered audit firms and their audits of issuers identifies six key areas of focus:

- Audit areas where deficiencies have been identified in previous inspection cycles, including internal control over financial reporting, assessing and responding to risks of material misstatement, and auditing accounting estimates, including fair value measurements;
- Audit areas affected by economic trends, including the effect of the strengthening U.S. dollar, the increasing merger and acquisition activity, the search for higher-yielding investment returns in a low interest rate environment, and the effect of the fluctuations in oil and natural gas prices;
- Audits of certain areas that may involve significant judgment from management and/or auditors, including the auditor’s evaluation of segment identification and disclosures, the auditor’s consideration of an entity’s ability to continue as a going concern, and evaluation of income tax accounting and disclosures;
- Implementation of PCAOB Auditing Standard (AS) 2410, *Related Parties* (currently AS 18);
- Audit procedures involving information technology, particularly auditors’ use of software tools, and procedures to assess and address risks of material misstatement posed by cybersecurity; and
- A firm’s system of quality control, including its policies and procedures for (1) identifying the “root causes” of audit deficiencies and positive quality events, (2) complying with required audit committee communications, including those communications related to independence, (3) monitoring and maintaining independence, (4) performing engagement quality reviews with due professional care, and (5) applying professional skepticism throughout the audit.

Brokers and Dealers Audits. The staff inspection brief for auditors of brokers and dealers also identifies six key areas of focus:

- Auditor independence;
- Financial statement audit areas where audit deficiencies were identified in past inspections, including revenue, the assessment and response to risks of material misstatement due to fraud, financial statement presentation and disclosures, and fair value measurements;
- Audit work performed under AS 2410, *Related Parties*, which became effective for audits of fiscal years beginning on or after December 15, 2014;
- Audit procedures on the supporting schedules to the financial statements;
- Procedures for attestation engagements: the examination of compliance reports and the review of the statements in exemption reports; and
- Engagement quality review.

PCAOB inspection rule amendments approved by the SEC

The SEC on July 11 [approved](#) amendments to PCAOB Rule 4003, *Frequency of Inspections*. The amendments provide for:

- Eliminating the triennial inspection requirement for registered public accounting firms that play a substantial role in audits but do not issue audit reports and replaces it with a requirement to inspect at least five percent of such “substantial role only” firms;
- Giving the PCAOB with the discretion to forego the inspection of a registered public accounting firm that has not issued any audit reports in two consecutive years; and
- Clarifying that Rule 4003(d) as amended applies only to the audits of issuers.

The amended rule is effective immediately and applies to the audits of all issuers, including audits of emerging growth companies.

PCAOB updates standard-setting agenda

The PCAOB on July 1 posted to its website an [updated standard-setting agenda](#). The PCAOB staff are currently drafting proposed standards on “Auditing Accounting Estimates, Including Fair Value Measurements” and “The Auditor’s Use of the Work of Specialists” and plan to recommend that the Board propose for public comment revisions to its current standards in the first quarter of 2017.

SEC

SEC proposes amendments to update and simplify disclosure requirements

The SEC, as part of its disclosure effectiveness review, on July 13 [proposed amendments](#) to eliminate redundant, overlapping, outdated, or superseded provisions, in light of subsequent changes to SEC disclosure requirements, U.S. Generally Accepted Accounting Principles (U.S. GAAP), International Financial Reporting Standards (IFRS), and technology. The SEC is also seeking input on certain disclosure requirements that overlap with U.S. GAAP to determine whether to retain, modify, eliminate, or refer them to the Financial Accounting Standards Board (FASB) for potential incorporation into U.S. GAAP.

The public comment period will remain open for 60 days following publication of the proposing release in the *Federal Register*.

CorpFin updates C&DIs

The SEC’s Division of Corporation Finance (CorpFin) updated the following sections of the Compliance and Disclosure Interpretations (C&DIs):

- Securities Act Sections – [New question 111.02](#) – “Exxon Capital” exchange offers. (Updated 7/11/16)
- Securities Act Forms – [New question 125.13](#) – “Exxon Capital” exchange offers. (Updated 7/11/16)
- Exchange Act Sections 13(d) and 13(g) and Regulation 13D-G Beneficial Ownership Reporting – [New question 103.11](#) – Discusses Hart-Scott-Rodino (“HSR”) Act exemptions and the ability of a shareholder to file on Schedule 13G. (Updated 7/14/16)
- Regulation S-K – [Revised and replaced question 140.02](#) regarding Item 507 of Regulation S-K; [withdrew question 240.04](#) – Selling Security Holders. (Updated 7/26/16)

IESBA issues new ethics standard for accountants

The International Ethics Standards Board for Accountants (IESBA)¹ on July 14 released a new standard, [*Responding to Non-Compliance with Laws and Regulations*](#). The standard sets out a framework to guide auditors and other professional accountants (PAs) in what actions to take in the public interest when they become aware of a potential illegal act, known as non-compliance with laws and regulations (NOCLAR) committed by a client or employer.

The standard provides a clear pathway for auditors and other PAs to disclose potential non-compliance situations to appropriate public authorities in certain situations without being constrained by the ethical duty of confidentiality. It also places renewed emphasis on the role of senior-level accountants in business in promoting a culture of compliance with laws and regulations and prevention of non-compliance within their organizations.

According to IESBA Technical Director [Ken Siong](#), “The standard fills a gap in jurisdictions where legislation or regulation does not address professional accountants’ responsibilities in these situations, and by providing helpful guidance it may well complement legislation or regulation in jurisdictions that do address it.” The standard will be effective on July 15, 2017, with early adoption permitted.

IAASB issues public survey to inform 2017-18 work plan

The International Auditing and Assurance Standards Board (IAASB)² on July 25 released a survey consultation, [*The IAASB’s Work Plan for 2017-2018 and Continuing Relevance of Its Strategic Objectives*](#). The IAASB plans to use feedback from the consultation in evaluating its priorities and allocating its resources for 2017-18.

IAASB Chairman Prof. [Arnold Schilder](#) explained that, through outreach and consultation, the IAASB believes they are already addressing the “most pertinent topics in the public interest” and are “prioritizing standard setting in relation to the fundamental topics of accounting estimates, professional skepticism, quality control, risk assessment, and group audits – while at the same time actively debating the implications for practitioners of developments in data analytics, integrated reporting, and emerging forms of external reporting.”

The survey highlights a number of other topics that could warrant IAASB attention and asks respondents for their views on how the topics should be prioritized. The IAASB acknowledges that current standard-setting projects will endure into 2017 and beyond unless the IAASB decides to modify its current work plan. The survey also asks whether the IAASB’s current strategic initiatives remain appropriate.

The survey is open for responses through September 30, 2016.

¹ The [IESBA](#) is an independent standard-setting board that develops and issues, in the public interest, high-quality ethical standards and other pronouncements for professional accountants worldwide. Through its activities, the IESBA develops the *Code of Ethics for Professional Accountants*, which establishes ethical requirements for professional accountants. The structures and processes that support the operations of the IESBA are facilitated by IFAC.

² The [IAASB](#) develops auditing and assurance standards and guidance for use by all professional accountants under a shared standard-setting process involving the [Public Interest Oversight Board](#), which oversees the activities of the IAASB, and the IAASB Consultative Advisory Group, which provides public interest input into the development of the standards and guidance. The structures and processes that support the operations of the IAASB are facilitated by IFAC.

CAQ comments on post-implementation review of auditing standards

The Center for Audit Quality (CAQ) on July 1 submitted a [comment letter](#) on the PCAOB's [Post-Implementation Review No. 2016-01](#), *Engagement Quality Review*. The PCAOB on April 6 issued a request for public comment on the post-implementation review of AS 7, *Engagement Quality Review* (AS 1220 under the PCAOB's reorganized standards).

The CAQ's comment letter focuses on the post-implementation review process rather than on the implementation of AS 7. In particular, the CAQ:

- Supports a post-implementation review process that includes: evaluating whether a rule or standard is accomplishing its intended purpose; understanding costs and benefits; identifying unanticipated consequences; obtaining and evaluating input from all stakeholders affected by the standard; allowing the auditing profession and other stakeholders either engaged in or benefitting from the financial reporting process an opportunity to inform the PCAOB whether rules and standards achieve stated objectives; analysis of data collected through the PCAOB inspection and enforcement programs; review of relevant academic literature; and focus group meetings to obtain input from interested parties and experts including audit firms, investors, public companies, and academics;
- Recommends that future post-implementation reviews include more details as to subsequent actions the PCAOB intends to take as a result of the process;
- Encourages the PCAOB to establish and publish a post-implementation review agenda, similar to the Office of the Chief Auditor's standard-setting agenda, to alert all relevant parties to rules and standards identified as potential candidates for future post-implementation reviews;
- Recommends that the PCAOB consider the appropriate timing for conducting its post-implementation review of a standard.

CAQ comments on business and financial disclosure required by Regulation S-K

On July 21, the CAQ submitted a [comment letter](#) on the SEC Concept Release, *Business and Financial Disclosure Required by Regulation S-K*. In the CAQ's view, a principles-based disclosure regime, supplemented with guidance or considerations on how to apply the principles, will promote the disclosure of meaningful and relevant information.

The CAQ also expresses its support in a disclosure regime that can be consistently applied to all registrants. Different reporting requirements for differently-sized registrants may result in unnecessary confusion and complexity in the disclosure framework. The flexibility offered by such a framework should encourage registrants to tailor disclosures to their facts and circumstances and reduce redundant and overlapping disclosures.

The CAQ encourages the SEC to conduct further extensive outreach and engagement with investors and other users of SEC filings to understand their views on how business and financial disclosures can be improved.

CAQ comments on supervision of audits involving other auditors

The CAQ on July 29 submitted a [comment letter](#) on the PCAOB's *Proposed Amendments Relating to the Supervision of Audits Involving Other Auditors and Proposed Auditing Standard – Dividing Responsibility for the Audit with Another Accounting Firm* (the "Proposal"). In this letter, the CAQ expresses agreement that current professional standards regarding the use of other auditors should be the subject of outreach and enhancement. Changes in the business environment, company organizational structures, accounting firm structures, financial reporting standards, and regulatory reporting requirements have all contributed to the need to revisit current standards.

The CAQ also believes there are opportunities to clarify the risk-based supervision model that is outlined in the Proposal.

- We are recommending that the PCAOB consider embedding flexibility into the standards to allow the lead auditor to vary the nature, timing, and extent of supervision based on the significance of the assessed risks of material misstatement being addressed by the other auditor, and the understanding of the knowledge, skill and ability of the other auditors who assist the engagement partner with supervision.
- The CAQ is also recommending that the Board consider making a distinction between an in-network and unaffiliated firm when considering the extent of supervision required by the lead auditor.
- We have also asked the PCAOB to consider the impact a firm's system of quality control has on the level of supervision and review of other auditors.

Highlights of May 2016 International Practices Task Force meeting now available

The CAQ has posted on its website [highlights](#) from the May 17 meeting of the International Practices Task Force (IPTF). The IPTF is a task force of the CAQ's SEC Regulations Committee.

The issues discussed during the meeting included:

- Monitoring Inflation in Certain Countries, including: South Sudan, Sudan, Venezuela, Belarus, Islamic Republic of Iran, Malawi, Ukraine, Yemen, and Argentina;
- New NYSE Rule Related to Interim Financial Information;
- Updating annual financial statements for retrospective accounting that is first reflected in a full set of interim financial statements, that are not needed to meet nine-month financial statement timeliness requirements under Item 8.A.5 of Form 20-F;
- More current interim financial statements provided on a local GAAP basis (i.e., other than U.S. GAAP or IFRS as issued by the International Accounting Standards Board (IFRS-IASB)), that is not needed to meet nine-month financial statement timeliness requirements under Item 8.A.5 of Form 20-F;
- More current interim financial information provided on a local GAAP basis (other than IFRS-IASB or U.S. GAAP), for an FPI that files its annual financial statements under IFRS-IASB; and
- Period to be covered for changes in internal control over financial reporting in the first 10-K filed by an issuer that was previously an FPI filing annual reports on Form 20-F.

The next IPTF meeting has been scheduled for November 17.

CAQ issues new 'Profession in Focus' videos

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

- [Episode 26](#) features Harvey L. Pitt, Chief Executive Officer and Managing Director at Kalorama Partners. A former SEC chairman, Pitt shares thoughts on the state of audit quality, the need for better use of technology in financial reporting, and how securities regulators are keeping up with rapid changes in the marketplace.
- [Episode 27](#) features CAQ Governing Board member Jeffrey Brown, Professor of Business and Dean of the College of Business at the University of Illinois at Urbana-Champaign. Professor Brown discusses the importance to any organization of getting independent perspective, the value of interaction between academic researchers and professionals, and the tightrope that audit committees must walk between executing core responsibilities and grappling with emerging issues.

Upcoming Events

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 17-20

NACD 2016 Global Board Leaders' Summit, Washington DC ([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 4

NACD Forum: "The Current Regulatory Landscape: What Inquiring Boards May Wish to Know," New York, NY ([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 and Technical Alert (PPTA) 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: aschumacher@thecaq.org.