PUBLIC POLICY & TECHNICAL ALERT

CAQ

June 2019

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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Upcoming Events

PCAOB

PCAOB updates Data and Technology project web page

The PCAOB updated its Data and Technology project web page with information on the project's objective, background, and status. The update includes details about staff activities and the PCAOB's Data and Technology Task Force.

Nayantara Hensel named PCAOB Chief Economist and ERA Director

The PCAOB announced that Dr. Nayantara Hensel has been named Chief Economist and Director of the Office of Economic and Risk Analysis (ERA). In this role, Dr. Hensel will advance the organization's economic analysis, research programs, and risk and other policy analysis. This research and analysis will inform PCAOB activities, including standard-setting, inspection, and enforcement, to achieve the most effective outcomes to further investor protection and enhance audit quality.

Dr. Hensel replaces Dr. Patricia Ledesma, the ERA's Acting Director since 2017. Dr. Ledesma joined the PCAOB in 2014 as Program Leader to build the Center for Economic Analysis. In that role, she worked to advance evidence-informed policy and foster economic research on auditing.

SEC

SEC adopts amendment to single issuer exemption for broker-dealers

The SEC adopted an amendment to an exemptive provision in the broker-dealer annual reporting rule under the 1934 Securities Exchange Act. The exemption provides that a broker-dealer is not required to engage an independent public accountant to certify the broker-dealer's annual reports filed with the SEC if, among other things, the broker-dealer's securities business has been limited to acting as broker (agent) for a single issuer in soliciting subscriptions for that issuer's securities.

The amended exemption provision will be effective on August 13, 2019.

SEC adopts amendments to improve the application of the auditor independence rules to loan provision

The SEC adopted amendments to the auditor independence rules relating to the analysis that must be conducted to determine whether an auditor is independent when the auditor has a lending relationship with certain shareholders of an audit client. The amendments are intended to more effectively identify debtor-creditor relationships that could impair an auditor's objectivity and impartiality, as opposed to certain more attenuated relationships that are unlikely to pose such threats.

Rule 2-01(c)(1)(ii)(A) of Regulation S-X (the "Loan Provision") generally provides that an auditor is not independent if that auditor is in a lending relationship with its audit client. In recent years, the SEC has become aware that, in certain circumstances, the existing Loan Provision may not have been functioning as it was intended.

The amendments will focus the analysis on beneficial ownership rather than on both record and beneficial ownership; replace the existing ten percent bright-line shareholder ownership test with a significant influence test; add a known through reasonable inquiry standard with respect to identifying beneficial owners of the audit client's equity securities; and exclude from the definition of audit client, for a fund under audit, any other funds that otherwise would be considered affiliates of the audit client under the rules for certain lending relationships.

The amendments will be effective 90 days after publication in the *Federal Register*.

SEC seeks public comment on ways to harmonize private securities offering exemptions

The SEC issued a concept release that reviews the framework for exempt offerings, including several exemptions from registration under the Securities Act of 1933 that facilitate capital raising. The concept release seeks comment on possible ways to simplify, harmonize, and improve this exempt offering framework to expand investment opportunities while maintaining appropriate investor protections and promote capital formation.

The SEC also released a staff report on the impact of Regulation Crowdfunding on capital formation and investor protection. The relevant findings of the report are discussed in the concept release.

The deadline for submitting comments on the concept release is September 24, 2019.

SEC statement on commencement of appointment process for the 2019-2024 PCAOB Board seat

The SEC has begun the process for appointing a PCAOB Board Member to the 2019-2024 term. The appointment process used by the SEC in 2017 will be followed to select the Board Member for the 2019-2024 term. This process is administered by the Office of the Chief Accountant (OCA) and is described on the OCA's website page.

Board Member Kathleen Hamm's term expires in October 2019. She is eligible for reappointment to the 2019-2024 term.

Individuals who would like to be considered for the PCAOB seat should submit their applications to the OCA by July 15, 2019.

SEC announces Kevin Zerrusen as Senior Advisor to the Chairman for Cybersecurity Policy

The SEC appointed Kevin Zerrusen to serve as Chairman Jay Clayton's Senior Advisor for Cybersecurity Policy. In this role, he will coordinate efforts across the agency to address cybersecurity policy, engage with external stakeholders, and help enhance the SEC's mechanisms for assessing cyber-related risks.

FASB

FASB proposes narrow-scope improvements to credit losses standard

The FASB issued Proposed Accounting Standards Update (ASU), *Codification Improvements to Topic 326: Financial Instruments – Credit Losses*. The proposed ASU would address issues raised by stakeholders during the implementation of ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*.

The proposed ASU aims to:

1. Clarify that an entity should include expected recoveries of the amortized cost basis previously written off or expected to be written off in the valuation account for purchased financial assets with credit deterioration (PCD). It also would clarify that recoveries or expected recoveries of the unamortized noncredit discount or premium should not be included in the allowance for credit losses.

2. Provide transition relief by permitting entities to adjust the effective interest rate on existing troubled debt restructurings using prepayment assumptions on the date of adoption of Topic 326 rather than the prepayment assumptions in effect immediately before the restructuring.

3. Extend the disclosure relief for accrued interest receivable balances to additional relevant disclosures involving amortized cost basis.

4. Clarify that an entity should assess whether it reasonably expects the borrower will be able to continually replenish collateral securing the financial asset to apply the practical expedient.

5. Clarify the guidance by removing the cross-reference to Subtopic 310-30, *Loans and debt securities acquired with deteriorated credit quality* in paragraph 805-20-50-1 and replacing it with a cross - reference to the guidance on PCD assets in Subtopic 326-20, *Measured at amortized cost*.

The deadline for submitting comments is July 29, 2019.

FASB moves toward approving accounting relief for contract modifications arising from reference rate reform

The FASB, during the June 19 Board meeting, took a step toward approving accounting relief for companies and organizations required to modify contracts as a result of new global reference rates.

The FASB tentatively decided that, for a contract that meets certain criteria, a change in that contract's reference interest rate would be accounted for as a continuation of that contract rather than the creation of a new contract. This decision applies to loans, debt, leases, and other arrangements.

Currently, trillions of dollars in loans, derivatives, and other financial contracts reference the London Interbank Offered Rate (LIBOR), the benchmark interest rate banks use to make short-terms loans to each other. Consequently, their related cash flows are tied to that rate. With global capital markets expected to move away from LIBOR towards more transaction-based reference rates, the FASB launched a broad project to address potential accounting concerns expected to arise from the transition. Additionally, in late 2018, the FASB added the secured overnight financing rate – or SOFR – as a permissible benchmark rate for hedge accounting purposes.

The FASB will discuss other hedging-specific reference rate issues at a public meeting in July.

FASB to consider delaying standards for private companies, non-profits, and smaller public companies

Chairman Russell Golden, speaking at the Institute of Management Accountants' Annual Conference, said that, in July, the FASB will consider whether it should extend implementation timelines for private companies and not-for-profit organizations as well as for smaller public companies; and if so, how "small public company" should be defined. As part of this process, the FASB will look at the effective dates of certain standards that are not yet effective to determine whether they should be amended to reflect a new philosophy.

FASB seeks public company input on segment reporting

The FASB is seeking public companies to participate in a study that focuses on potential improvements to the segment disclosure requirements.

This is the FASB's second study on segment reporting and focuses on the information that is disclosed by each reportable segment. The first study, undertaken in 2018, focused on improving the aggregation criteria and the process for determining the reportable segments.

For this study, the FASB seeks public companies that apply the disclosure requirements in Topic 280, *Segment Reporting*. Participants in the study will be asked to provide information on the operability of various potential improvements to the segment disclosure requirements and to identify any potential unintended consequences. Feedback obtained from the study will help inform the FASB about the costs and benefits of the different ideas.

International

Tom Seidenstein to lead the IAASB

Thomas R. Seidenstein has been named the new chair of the IAASB for a three-year term commencing July 1, 2019. He succeeds Prof. Arnold Schilder, who has led the IAASB since 2009.

IASB consults on amendments to aid implementation of IFRS 17

The IASB issued an exposure draft of proposed amendments to IFRS 17, *Insurance Contracts*, for public consultation. The aim of the amendments is to continue supporting implementation by reducing the costs of implementing the standard and making it easier for companies to explain their results when they apply the standard.

The exposure draft does not change the standard's fundamental principles or reduce the usefulness of information for investors. In the light of the proposed amendments, the IASB is also proposing to defer the standard's effective date by one year – to 2022.

The deadline for submitting comments is September 25, 2019.

FSB holds roundtable on external audit

The Financial Stability Board (FSB) held the latest in a series of roundtables on External Audit in Toronto on June 6-7. The roundtable's objective was to engage in constructive dialogue regarding ways to promote international financial stability by enhancing public confidence in auditors and the quality of audits, especially for systemically important financial institutions.

Roundtable participants considered the following areas:

- The recurrence, level and root causes of audit inspection findings identified by The International Forum of Independent Audit Regulators (IFIAR) members in their individual inspections of audit firms affiliated with the global networks;
- Observations from initial audits of expected credit loss estimates under IFRS 9, *Financial Instruments*, including the audit work needed to assess the related governance and controls, management judgments and assumptions, and the resulting presentation and disclosures;
- The global networks' progress in preparing for the implementation of IFRS 17, *Insurance Contracts,* and the related audits;
- Support for IFIAR in promoting collaboration in regulatory activity to foster the effectiveness of audit oversight globally;
- Effective avenues to strengthen the dialogue between the financial sector and the global networks, as a means to inform strong financial sector policies to advance audit quality and promote international financial stability;
- Characteristics of audit services, particularly for financial statement audits of systemically important financial institutions, and the potential implications for the role of financial reporting in international financial stability; and
- The importance of a robust and proactive approach by the global networks in continuing to improve audit quality.

EC issues new rules to support digitalization and transparency of financial reports

The European Commission (EC) issued new rules to support the digitalization of corporate reporting and to achieve greater transparency of the yearly information disclosed by companies listed in the European Union capital markets. The new European Single Electronic Format will make companies' financial records more readable and accessible.

Under the new rules, from January 2020 all listed companies will need to finalize their annual financial reports using up-to-date digitalized business reporting systems (XHTML and iXBRL). The move also will facilitate the availability of key financial information in all EU official languages.

The new provisions build on financial transparency rules already agreed to by the European Parliament and Member States. They will be updated on a yearly basis to reflect possible updates to the IFRS taxonomy.

IOSCO urges authorities to use existing standards to address cyber risk

The Board of the International Organization of Securities Commissions (IOSCO) issued a final report that provides an overview of three internationally recognized cyber standards and frameworks used by IOSCO members. It also identifies potential gaps in the application of these standards and seeks to promote sound cyber practices across the IOSCO membership.

The report is intended to serve as a resource for financial market regulators and firms, raise awareness of existing international cyber standards and frameworks and encourage the adoption of good practices to protect against cyber risk – an important threat to financial markets today.

AICPA

AICPA proposed auditing standard tackles evolution of audit evidence

The AICPA's Auditing Standards Board (ASB) issued an exposure draft of a Proposed Statement on Auditing Standards (SAS), *Audit Evidence*, to supersede SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*, as amended, section 500, *Audit Evidence*, and amend various other AU-C sections in AICPA *Professional Standards*.

The exposure draft addresses the evolving nature of business, audit services and issues that have arisen since the existing AU-C section 500 was originally issued. The issues include:

- The use of information as audit evidence when emerging technologies are used by preparers and auditors (for example, audit data analytics and use of blockchain);
- The application of professional skepticism;

- The expanding sources of information to be used as audit evidence; and
- The accuracy, completeness, relevance and reliability of audit evidence.

The exposure draft includes a recommendation to shift the focus of the standard, including its objective to concentrate on helping the auditor assess whether sufficient and appropriate audit evidence has been obtained when the information is obtained from sources not available in the past. The change is proposed to be accomplished by establishing a multi-dimensional consideration of attributes and factors to be used in evaluating audit evidence obtained from any source and regardless of how the auditor acquired the information, including the use of automated tools and techniques.

The deadline for submitting comments is September 18, 2019.

AICPA proposes amendments to the description of materiality

The AICPA's ASB issued an exposure draft of a Proposed Statement on Auditing Standards, and a Proposed Statement on Standards for Attestation Engagements, both titled *Amendments to the Description of the Concept of Materiality.* The exposure draft would amend various AU-C and AT-C sections in AICPA *Professional Standards*.

The ASB's current description of the concept of materiality is consistent with the IASB's and the IAASB's definitions of materiality. The proposed amendments would align the materiality concepts discussed in AICPA *Professional Standards* with the definition of materiality used by the U.S. judicial system, PCAOB auditing standards, SEC, and FASB.

The deadline for submitting comments is August 5, 2019.

AICPA considers aligning SSARS with international standards

The AICPA's Accounting and Review Services Committee (ARSC) issued an exposure draft of a Proposed Statement on Standards for Accounting and Review Series (SSARS), *Materiality in a Review of Financial Statements, Adverse Conclusions, and Special Purpose Frameworks* to amend AR-C sections 60, 70, 80, and 90 in AICPA *Professional Standards*.

The exposure draft further converges AR-C section 90, *Review of Financial Statements*, with International Standard for Review Engagements (ISRE) 2400 (Revised), *Engagements to Review Historical Financial Statements*. The ARSC believes it is important for the SSARS's literature to be as closely converged with ISRE 2400 (Revised) as possible to facilitate an accountant's ability to perform and report on engagements and mitigate confusion regarding the level of assurance obtained in accordance with either set of standards.

In addition, even though there are significant differences between an audit engagement and an engagement performed in accordance with SSARSs, certain concepts, such as materiality, are consistent regardless of the level of services performed on the financial statements. The exposure draft proposes to better align those concepts in the SSARSs.

The deadline for submitting comments is September 20, 2019.

Other Developments

House subcommittee considers PCAOB-related draft legislation

The House Financial Services Committee's Subcommittee on Investor, Entrepreneurship and Capital Markets held a hearing on eight legislative proposals designed to bolster regulators' enforcement tools against securities law violators. Three of the draft bills deal with the PCAOB:

- *Holding Foreign Companies Accountable Act*: The draft bill would require the SEC to prohibit U.S. public companies from trading on an exchange or an alternative trading system if it retains a foreign public accounting firm that the PCAOB is unable to inspect. The SEC can end the trading prohibition once the company certifies that it has retained a public accounting firm that the PCAOB is able to inspect. The draft bill also would require an issuer to disclose whether it is state-owned or government-controlled.

- *To establish a whistleblower program at the PCAOB*: The draft bill would establish a whistleblower program at the PCAOB that is similar to the program Congress established at the SEC under the Dodd-Frank Act. If eligible for a reward upon the successful completion of a PCAOB disciplinary action, whistleblowers may be incentivized to come forward when they suspect violations of the Sarbanes-Oxley Act, the rules of the PCAOB and the SEC, and other laws, rules, and professional standards governing the audits of public companies, brokers, and dealers. These whistleblowers also would be protected from retaliation by their employer.

- *PCAOB Enforcement Transparency Act*: The draft bill would make PCAOB hearings and all related notices, orders, and motions, open and available to the public unless otherwise ordered by the Board. The PCAOB procedure would then be similar to SEC Rules of Practice for similar matters, where hearings and related notices, orders, and motions are open and available to the public.

Senate, House bills would open U.S.-listed Chinese companies to SEC, PCAOB oversight

A bipartisan group of U.S. senators and representatives introduced the Ensuring Quality Information and Transparency for Abroad-Based Listings on our Exchanges (EQUITABLE) Act

(S. 1731 / H.R. 3124). The bill would increase oversight of Chinese and other foreign companies listed on American exchanges and delist firms that are out of compliance with U.S. regulators for a period of three years.

According to the summary of the legislation, the EQUITABLE Act would delist foreign companies that do not comply with U.S. accounting and oversight regulations from U.S. exchanges, subject to a grandfather provision, in order to avoid sudden losses to existing shareholders. Prior to the onset of this provision, non-compliant companies would be subject to a robust disclosure regime in order to inform investors of their risk and to price this uncertainty into the market. The bill also would place an initial listings ban on foreign companies seeking to list on U.S. exchanges that retain the services of public accounting firms whose audit reports have been withheld from U.S. regulators.

Rep. Budd introduces bill to delay CECL implementation

Rep. Ted Budd (R-N.C.) introduced H.R. 3182, the CECL Consumer Impact and Study Bill, which would delay compliance with the FASB's Accounting Standards Update (ASU) 2016-13, *Topic 326* and ASU 2018-19, *Codification Improvements to Topic 326, Financial Instruments - Credit Losses* for up to one year ("Current Expected Credit Losses" or "CECL").

The bill would require the SEC and federal financial regulators to conduct a quantitative study of (1) the potential impact that the implementation of Current Expected Credit Losses may have on the availability of credit; (2) the potentially disproportionate impact that the implementation of CECL may have on financial institutions; (3) the potential impact that the implementation of CECL may have on the decisions made by investors; and (4) the potential competitive impact that the implementation of CECL may have on institutions in the U.S. as a result of differing international accounting standards used to measure credit loss.

The bill also would require the SEC and federal financial regulators to conduct a cost-benefit study on the potential costs and benefits of the impact of CECL on non-financial institutions, the insurance industry (including reinsurance), and government-sponsored enterprises.

The reports on both studies would be due within one year of the bill's enactment.

Senate confirms Allison Lee to SEC

The Senate confirmed Allison Lee to serve as an SEC commissioner for a term expiring on June 5, 2022. She will fill the vacant seat previously held by former Commissioner Kara Stein.

CAQ Updates

EY's Grier and BDO's Berson tapped to lead the CAQ Governing Board

The CAQ Governing Board has elected new leadership. Effective October 1, 2019, Kelly Grier, U.S. Chairman and Managing Partner and Americas Managing Partner at EY, will become the Governing Board's Chair. Wayne Berson, U.S. CEO at BDO USA, LLP and Global Chairman at BDO International, will serve as Vice Chair.

CAQ Governing Board Chairs and Vice Chairs are elected to two-year terms.

Upcoming Events

July 16-18 ICGN Annual Conference, Tokyo, Japan (Link)	**August 14** SEC Government-Business Forum, Omaha, NE (Link)	**September 21-24** NACD Global Board Leaders' Summit, Washington, DC (Link)
July 22-26 IASB Board Meeting, London, UK (Link)	**August 15-16** AICPA Cybersecurity Advisory Services Certificate Conference, New York, NY (Link)	**September 23-24** PLI 15th Annual SEC Reporting & FASB Forum for Mid-sized & Smaller Companies, Las Vegas, NV (Link)
July 30-31 AICPA SOC for Cybersecurity Certificate, Denver, CO (Link)	**August 20** Accounting Today Webinar: The Future of Audit (Link)	**September 23-27** IASB Board Meeting, London, UK (Link)
August 6-7 AICPA Cybersecurity Advisory Services Certificate Conference, Durham, NC (Link)	**September 12** KPMG/NACD Quarterly Audit Committee Webcast (Link)	**October 15-16** ICGN Conference, Miami, FL (Link)
August 10-14 AAA Annual Meeting, San Francisco, CA (Link)	**September 18** AICPA Conference: Blockchain Implications for Audit & Assurance Services, Chicago, IL (Link)	**October 21-25** IASB Board Meeting, London, UK (Link)

October 23-25 CII 2018 Fall Conference: New York, NY (Link)	**November 11-12** AICPA Oil & Gas Conference, Denver, CO (Link)	**December 5-6** AICPA Construction & Real Estate Conference, Nashville, TN (Link)
October 24 NACD Webcast: Why Data Privacy Matters in a Public World (Link)	**November 18-22** IASB Board Meeting, London, UK (Link)	**December 9-11** AICPA Conference on Current SEC and PCAOB Developments, Washington, DC (Link)
November 6-8 AICPA Women's Global Leadership Summit, San Diego, CA (Link)	**November 18-19** SIFMA Annual Meeting, Washington, DC (Link)	**December 9-12** IASB Board Meeting, London, UK (Link)
November 11-12 PLI 35th Annual SEC Reporting & FASB Forum, Dallas, TX (Link)	**December 2-3** PLI 35th Annual SEC Reporting & FASB Forum, San Francisco, CA (Link)	**December 16-17** PLI 35th Annual SEC Reporting & FASB Forum, New York, NY and Webcast (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.

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Questions and comments about the PPTA can be addressed to: info@thecaq.org.

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