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April 28, 2020

By email: [rule-comments@sec.gov](mailto:rule-comments@sec.gov)

U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

**Re: Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information; File Number S7-01-20**

Dear Office of the Secretary:

The Center for Audit Quality (CAQ) is an autonomous public policy organization dedicated to enhancing investor confidence and public trust in the global capital markets. The CAQ fosters high quality performance by public company auditors; convenes and collaborates with other stakeholders to advance the discussion of critical issues requiring action and intervention; and advocates 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.

The CAQ appreciates the opportunity to share our views and provide input on the Securities and Exchange Commission's ("Commission" or "SEC") Release No. 33-10750, *Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information* (the "Proposal" or the "Proposed Rule").<sup>1</sup> This letter represents the observations of the CAQ's SEC Regulations Committee but not necessarily the views of any specific firm, individual, or CAQ Governing Board member.

Since auditors play an important role in enhancing the quality, rigor, and reliability of financial information disclosed in Commission filings, the profession has a strong interest in the success of the Commission's Disclosure Effectiveness Initiative. Additionally, when a filing includes audited financial statements, we are required under our professional standards to read the other information contained in the filing and take certain action when such information, or the manner of its presentation, is materially inconsistent with information, or the manner of its presentation,

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<sup>1</sup> Proposed Rule; Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information; Release Nos. 33-10750 and 34-88093; File No. S7-01-20.



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appearing in the financial statements.<sup>2</sup> Therefore, we provide our comments through the lens of the public company audit profession.

### **Overall Comments**

We are generally supportive of the Commission's efforts to modernize, simplify and enhance the financial disclosure requirements in Regulation S-K and we appreciate the Commission's thoughtful consideration of the input provided in our comment letter to SEC Release No. 33-10064, *Business and Financial Disclosure Required by Regulation S-K* ("previous comment letter").<sup>3</sup> We commend the Commission's efforts to leverage technology and its consideration of changes in reporting requirements under U.S. Generally Accepted Accounting Principles (U.S. GAAP) and International Financial Reporting Standards (IFRS) in identifying and eliminating duplicative or redundant requirements. In that vein, we do not object to the elimination of Item 301, *Selected Financial Data*, and Item 302, *Supplementary Financial Information*. We also are supportive of the Commission's efforts to modernize Regulation S-K using a principles-based approach. As stated in our previous comment letter, we believe this approach allows registrants to more effectively communicate material information to investors that is focused, relevant, and appropriate for a registrant's particular facts and circumstances. Accordingly, we agree that clear and understandable disclosure objectives articulated within each item of Regulation S-K are important to define the parameters in which disclosures should be made. Unless otherwise specified, our comments outlined below apply broadly to all categories of registrants, including Foreign Private Issuers.

### **Management's Discussion and Analysis (MD&A) – Critical Accounting Estimates**

The Commission proposes to amend Item 303(a) to explicitly require disclosure of Critical Accounting Estimates (CAEs), including, to the extent material, 1) why the estimate is subject to uncertainty, 2) how much each estimate has changed during the reporting period, and 3) the sensitivity of the reported amounts to the material methods, assumptions, and estimates underlying the estimate's calculation. As stated in our previous comment letter, we support the requirement to disclose CAEs and the process employed by management in creating the estimates. We also support the principles-based approach to CAE disclosures and the Commission's plan to include an instruction that the disclosures should supplement but not duplicate U.S. GAAP.

To achieve the intended objective of this amendment, we recommend the Commission clarify certain aspects of the proposed CAE disclosure requirements as follows:

- **Sensitivity Disclosures.** The level of the sensitivity disclosure required by the Proposal may be difficult for management to prepare in a way that is useful to investors. Most accounting estimates are developed using a number of interrelated assumptions. Because of these interrelationships, it often would be difficult or less meaningful to isolate the sensitivity of a particular assumption. As a result, the costs of disclosing the

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<sup>2</sup> Public Company Accounting Oversight Board ("PCAOB") Auditing Standard ("AS") 2710, *Other Information in Documents Containing Audited Financial Statements*, paragraph 4.

<sup>3</sup> [CAQ comment letter](#) on *Business and Financial Disclosure Required by Regulation S-K*, SEC Release No. 33-10064, July 21, 2016, page 2.



sensitivity information as currently proposed may outweigh the benefits. We recommend the SEC clarify that a quantified sensitivity analysis would be required only when changing a particular underlying method, assumption or estimate is 1) relevant and practicable to quantify considering its interrelationship with other underlying variables, 2) reasonably likely to occur, and 3) the resulting change in the CAE would be material.

- **Reporting Periods.** It is unclear in the Proposal whether the registrant should disclose how much each estimate has changed during each reporting period presented in the filing (e.g., for each of the two or three fiscal years presented) or only the most recent reporting period. As such, we recommend the Commission clarify the reporting periods for changes in the estimate.

### **Foreign Private Issuers**

The Proposal includes changes to Form 20-F Item 5.E. regarding CAEs stating, “A registrant ***that does not apply in its primary financial statements IFRS as issued by the IASB*** must discuss information about its critical accounting estimates.” The bolded part of this sentence appears redundant as Instruction 5 to Item 5 already indicates that a registrant does not need to repeat information contained in its financial statements that comply with IFRS as issued by the IASB. We suggest the SEC eliminate the bolded part of the sentence to simply state “A registrant must discuss information about its critical accounting estimates.” Eliminating this language also would prevent issues should IFRS requirements change in the future.

### **Auditor’s Responsibility for Fourth Quarter Information Voluntarily Provided.**

Regarding the proposed elimination of Item 302(a), we observe that registrants may still elect to *voluntarily* present summary quarterly information, including fourth quarter information within their annual reports. In these circumstances, the auditor’s responsibility relating to that information is not clear. Specifically, paragraph 6 of AS 4105, *Reviews of Interim Financial Information*, requires auditors to review disclosures that are *required* to be included in a filing but does not specifically address the auditor’s responsibility concerning disclosures that are *voluntarily* provided. We do not object to the elimination of Item 302(a) as proposed, but we recommend the SEC coordinate with the PCAOB to amend auditing standards as necessary in order to provide clarity regarding the auditor’s responsibility relating to fourth quarter information that is voluntarily provided.

### **Transition Guidance**

We support the SEC’s inclusion of an optional transition period paired with a mandatory transition date to allow preparers flexibility in complying with any final rule.

### **SEC Staff Guidance**

We recommend the SEC staff undertake a comprehensive review of existing guidance regarding the Regulation S-K disclosures discussed in the Proposal to clarify which aspects will continue to apply and, if so, how they will apply in the context of any final rule. While it may be clear that certain existing staff guidance will no longer apply (because for example it has been addressed in the final rule), it may not be clear how certain other guidance is applicable (e.g., SEC Interpretive Releases). Providing this clarity prior to the effective date of any final rule likely would reduce uncertainty and thus implementation costs and efforts.



## **Sustainability and Environmental, Social and Governance (ESG) Disclosures**

We continue to observe strong interest in ESG disclosures from large institutional investors and we also have observed commitments from senior business leaders to disclose this information. Further, we recognize the Commission is engaging on environmental and climate-related disclosures, and we support those efforts.<sup>4</sup> We believe these and other ESG disclosures would provide investors and other stakeholders more meaningful information if they were subject to a disclosure framework centered on principles-based objectives that emphasizes materiality as a touchstone for the disclosure.

ESG disclosure frameworks and standards have been developed both globally and domestically. Some of these frameworks and standards, which are used voluntarily by some registrants, address such topics as energy and water management, hazardous waste, product safety, ethics and materials sourcing. As the Commission continues to engage on this topic, it should consider whether there is broad-based support from investors for a particular framework or standard, or whether flexibility to choose a framework or standard is preferred.

We also recommend the Commission weigh the costs and benefits of disclosing ESG information. As we have observed that some companies are voluntarily seeking assurance from auditors on their ESG information, the Commission also may consider seeking investor and other stakeholder input as to the value of auditor involvement in these disclosures and how companies can best present such information.

\* \* \*

We appreciate the opportunity to comment on the questions raised in the Proposal. As the Staff and Commission gather feedback from preparers, users and other interested parties, we would be pleased to discuss our comments or answer any questions that the Staff or Commissioners may have regarding the views expressed in this letter. Please address questions to Annette Schumacher ([aschumacher@thecaq.org](mailto:aschumacher@thecaq.org)).

Sincerely,

A handwritten signature in black ink that reads "Catherine Ide".

Catherine Ide  
Vice President, Professional Practice

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<sup>4</sup> See Chairman Clayton's January 30, 2020 [statement](#).



cc:

**SEC**

Jay Clayton, Chairman  
Allison Lee, Commissioner  
Hester M. Peirce, Commissioner  
Elad L. Roisman, Commissioner  
William H. Hinman, Director, Division of Corporation Finance  
Lindsay McCord, Acting Chief Accountant  
Patrick Gilmore, Acting Disclosure Review Program Director  
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