
Regulators Discuss Accounting and Auditing Developments at 2016 AICPA Conference

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This year's American Institute of Certified Public Accountants Conference on SEC and PCAOB Developments, held on December 5-7, echoed several themes from prior AICPA conferences regarding regulatory priorities of interest to audit committees. The significant discussion topics included:

- *Internal Control over Financial Reporting (ICFR)*. Consistent with the SEC's continued emphasis on ICFR, many speeches at this year's conference focused on ICFR. As newly-appointed SEC Chief Accountant [Wesley Bricker](#) noted, "it is hard to think of an area more important than ICFR to [the SEC's] mission of providing high-quality financial information that investors can rely on. If left unidentified or unaddressed, ICFR deficiencies can lead to lower-quality financial reporting and ultimately higher financial reporting restatement rates and higher cost of capital." New Deputy Chief Accountant [Marc Panucci](#) echoed the importance of ICFR by referencing the SEC Division of Enforcement's recent sanctions against a company and individuals for "an inadequate evaluation of the severity of an identified control deficiency." (See prior [post](#).) In light of the importance of ICFR to investors and the SEC, Mr. Panucci again encouraged management, audit committees and auditors to regularly engage in a dialogue regarding ICFR assessments.
- *Audit Committees*. Members of the SEC's Office of the Chief Accountant also commented more broadly on the important role of the audit committee. As a "critical gatekeeper" in the financial reporting process, Mr. Bricker advised that "[a]udit committees must stay current on emerging issues, whether financial, control, or disclosure related, through continuing education and other means. In addressing certain important issues, some audit committees may need expert advisors as they carry out fully their responsibilities." In discussing the importance of the audit committee's role in overseeing the external auditor, Mr. Bricker offered the following list of questions as a resource for generating a dialogue with a company's external auditor:
 - If you as the auditor were in management's shoes and solely responsible for preparation of the company's financial statements, would they have in any way been prepared differently?

- If you as the auditor were in an investor's shoes, would you believe that you have received the information essential to understanding the company's financial position and performance?
- Is the company following the same internal control over financial reporting and internal audit procedures that would be followed if you were in the CEO's shoes?
- Are there any recommendations that you as the auditor have made and management has not followed?

Mr. Bricker also suggested that corporate procurement policies and processes might be inappropriate if applied to auditor selection, retention and compensation decisions. He said that audit committees should "work with other board committees as needed to monitor that important corporate objectives, such as cost reduction plans, are not unintentionally implemented in ways that would be at cross purposes with management meeting their financial reporting responsibilities or the external auditor's appropriate audit scope, engagement terms, and compensation."

- *New and Revised Accounting Standards.* Further emphasizing the importance of effective ICFR, Mr. Bricker advised that "updating and maintaining internal controls" will be of particular importance over the next several years as companies implement a number of new and revised accounting standards, including with respect to revenue recognition, leases, financial instruments and credit losses. Effective ICFR will be essential to ensuring that such new standards are timely implemented with useful, appropriate disclosures. Focusing on the new revenue recognition standard (ASC 606), which takes effect for public organizations' annual reporting periods beginning after December 15, 2017, Mr. Bricker noted that since last year's conference, where he "said the overall state of readiness may be lagging, clear progress has been made by preparers, but there is more to do." Citing an October survey, Mr. Bricker noted that 8% of companies had not started an initial assessment of the new revenue recognition standard, 75% were still assessing the impact of the new standard, and 17% were implementing the new standard. For companies where implementation is lagging, auditors, audit committees, and preparers should discuss the reasons for the delay and disclose to investors the status of implementation. He also suggested that companies may wish to incorporate the anticipated effects of the new standard in their investor outreach activities to timely absorb input from market participants.
- *Auditor Independence.* Visiting another recurrent topic, auditor independence, Mr. Bricker cautioned that auditors must exercise professional judgment and common sense to avoid independence issues in circumstances where auditors may be asked to provide feedback to management regarding the impact of new accounting standards on a company's accounting policies, processes, and controls. Mr. Panucci encouraged audit committee members to closely monitor non-audit services provided by a company's external audit firm. Throughout the delivery of such services, audit committees should be on the lookout for engagement "scope creep" to ensure that the independence of the company's external auditor does not become impaired. As discussed at AICPA conferences in prior years, Mr. Panucci cited the growth in audit firms' consulting practices and how that might impact

independence and audit quality as an important area to monitor. He noted that the PCAOB's current strategic plan identifies firms' multi-disciplinary structure as an "emerging threat" that it will continue to monitor.

- *Non-GAAP Measures.* Following up on SEC Chair Mary Jo White's remarks at last year's conference regarding non-GAAP measures and the SEC's focus on non-GAAP measures throughout 2016, Mr. Bricker advised that "there is more progress for companies to make," including with respect to the appropriateness and prominence of non-GAAP measures and the effectiveness of disclosure controls and procedures. Mr. Bricker encouraged audit committees to engage with management to understand management's judgments in the "design, preparation, and presentation of non-GAAP measures and how those measures might differ from approaches followed by other companies." Audit committees should evaluate closely non-GAAP adjustments that depart from the business reality, such as measures that would "smooth earnings over time, accelerate unearned revenues, or defer incurred expenses."
- *International Financial Reporting Standards (IFRS).* Mr. Bricker indicated that the possible future use of IFRS for domestic issuers is unlikely "at least for the foreseeable future." He did "strongly encourage the FASB and IASB to continue to work together to eliminate differences between their standards where such efforts will strengthen the standards" He also said that it is worth continuing to consider former Chief Accountant Jim Schnurr's proposal at a prior conference to allow U.S. issuers to supplement GAAP financial statements with IFRS-based information.
- *PCAOB Standard-Setting Activities.* Mr. Bricker, Mr. Panucci, and PCAOB Chair [James Doty](#) commented on the efforts undertaken by the PCAOB to "shore up the critical role of the audit in our markets," including updates to auditing standards, improvements in the PCAOB's standard-setting approach, and enhancements to the risk-based approach for inspections. Regarding changes to the PCAOB's standard-setting process, Mr. Panucci noted that "[t]he SEC staff has seen positive changes to date and is committed to working with the PCAOB as it continues the implementation of its changes." Chair Doty noted that "[t]he PCAOB is also nearing completion of a project to make the auditor's report more useful and informative to investors and other financial statement users," though he did not commit to a PCAOB board vote on the proposed standard by the end of the year as was contemplated when the PCAOB repropose the standard in May. (See previous [post](#).) Meanwhile, Mr. Bricker commended the PCAOB on its revised standard-setting approach and its progress on the auditor's reporting model, though he urged the PCAOB to "continue to work towards advancing and finalizing other important and challenging projects on its standard-setting agenda, including auditing accounting estimates."

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