SEC Chief Accountant Addresses 2018 Baruch College Financial Reporting Conference

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In a speech delivered at last week's 2018 Baruch College Financial Reporting Conference, SEC Chief Accountant Wes Bricker discussed objectives of financial reporting and its importance to the markets. Mr. Bricker revisited several well-established themes and offered some guidance for audit committees with regards to trending financial reporting considerations. He also commented on developments in audit quality and the continued evolution of the auditing profession.

As in prior remarks, Mr. Bricker emphasized the importance for companies to focus on successfully and timely implementing several new accounting standards, including the new leases and credit losses standards, which follow the new revenue recognition standard under which calendar year end public companies are now reporting revenue from contracts with customers. Addressing the SEC staff's recent Staff Accounting Bulletin No. 118 guidance (see our prior post), Mr. Bricker stated that "[t]he staff expects companies to act in good faith to complete the accounting" and suggested that as companies work to complete the accounting for the recent Tax Cuts and JOBS Act, they should provide investors with "insight through the disclosures described in SAB 118 about the status of a company's accounting for the effects of income tax reform during the measurement period."

Turning to non-GAAP measures, Mr. Bricker suggested that as part of their required disclosure controls and procedures, companies typically should have "appropriate governance practices regarding the measures and policies and controls that prevent error, manipulation, or mischief with the numbers, including a policy that addresses how any changes in the non-GAAP measure will be reported and how corrections of errors will be evaluated." In this regard, he highlighted that audit committees "can play an important role in understanding whether—and how and why—management uses any supplemental scorecards in understanding and tracking results and how that supplemental information may be used in addition GAAP financial statements in the company's public reporting." He suggested that audit committees should "clearly understand non-GAAP measures presented to the public—and . . . take the time and effort in their financial reporting oversight role to review with management the preparation, presentation, and integrity of those metrics," noting that engaging in such activities indicates a strong compliance and reporting culture.

Mr. Bricker also flagged market risk information as another area where audit committees can exert a positive influence on disclosure quality and advised that audit committees should be “attentive to disclosures regarding changes in market risks.” In this regard, Mr. Bricker observed the recent rise in general market interest rates and emphasized “the importance of management’s attention and financial reporting oversight of the disclosures companies make to investors about material risks in this area.” As Mr. Bricker described, for some businesses, “changes in the liquidity in the markets, the level and volatility of market prices and rates, including for debt and equity investments, market indices, or business and other sentiments that affect the markets,” can have a significant impact on their financial results.

Expanding beyond the role of management and audit committees in maintaining high quality financial reporting, Mr. Bricker commented on auditor independence and more broadly discussed the role of audit firm governance and culture. Analogizing to the need for auditors to continually “monitor and assess their maintenance of [their] independence from their audit clients,” Mr. Bricker indicated that regulators also “need to monitor and assess [their] auditor independence rules.” As an example, he highlighted the SEC’s May 2 request for public comment on a proposed rulemaking “to address certain substantial practical challenges to compliance” related to the “Loan Provision” part of the auditor independence rules. (See SEC Release No. 33-10491)

Discussing the importance of firm culture in the context of an evolving audit profession and related improvements in audit quality, Mr. Bricker described a spectrum of cultural maturity and commented on “human solutions and structural changes” that the largest accounting firms are implementing “to foster audit quality and safeguard against noncompliance threats and the resulting costs to the reputation of the firm, its network, and the audit profession generally.” Such changes at audit firms include appointing independent directors or independent advisory council members and are designed with a view toward satisfying US and global expectations for quality and risk management. As Mr. Bricker stated, “it is critical that the auditing profession continually look in the mirror and assess its conscience” to ensure that it is earning the public’s confidence and trust in audits. “Taking a fresh look at governance and culture as part of firm-wide risk management,” Mr. Bricker noted, “is one way US firms can take steps to meet the high standards expected of accountants.” Mr. Bricker also noted that such governance and culture considerations “can be insightful to audit committees in overseeing the external audit relationship.”

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