

## FEATURED TOPICS FROM THE 2018 AICPA CONFERENCE ON CURRENT SEC AND PCAOB DEVELOPMENTS

The annual AICPA Conference on Current SEC and PCAOB Developments (the “Conference”) was held in December and featured discussions by regulators and standard setters on a broad range of accounting, financial reporting, and auditing-related topics. The Conference focused on changes such as new standards and emerging technology, with speakers also commenting on practical responses to these developments and preparing for what’s next.

Highlights of the Conference included the following:

### Revenue Recognition

Unsurprisingly, the new revenue standard was a hot topic at the conference and a focus for the SEC staff. The staff acknowledged that the application of reasonable judgment is inherent to implementing the new standard, but could also result in diversity of practice, which they are monitoring.

- The staff will continue to focus on areas of significant judgment when reviewing filings such as: (1) The identification of performance obligations; (2) Determining whether an entity is acting as a principal versus an agent; (3) Determining the timing of revenue recognition; (4) Determining the appropriate disaggregation of revenue for disclosure.
- The staff highlighted two recent pre-filing consultations related to the new standard, which were representative of areas of significant judgment: (1) principal vs. agent and (2) the identification of performance obligations.
  - **Principal vs. agent:** The first consultation considered whether a distributor is acting as a principal or an agent when the manufacturer that creates the goods ships directly to the end customer. The staff did not object to the registrant’s conclusion that it was the principal because it controlled the goods before delivery to the retailer, even though it did not obtain physical possession. The conclusion that the registrant obtained control is subject to significant judgment, considering factors such as the specific terms of the agreement, content of marketing materials, control over pricing, and obligation to satisfy customer identified problems.
  - **Identification of performance obligations:** The second consultation considered whether software to prepare patent applications and a service allowing their customers to submit the applications should be considered separate performance obligations. In this circumstance, the registrant asserted that customers purchasing their software product were seeking a combined solution, which could not be satisfied without providing both the software and the service and, as such, the promises in the contract comprised a single performance obligation. In this instance, the staff objected to the registrant’s conclusion on the basis that the service was not required for the customer to obtain utility from the software. As such, the promises would not significantly affect each other and would not be considered highly interdependent or highly interrelated.

#### **Riveron Insight**

*Preparers should remember that although these evaluations involve significant judgment, the resulting accounting conclusions should be consistent in situations where facts and circumstances are the same or substantially similar.*

## Leases

The SEC and FASB staff emphasized that the effective date of the new lease standard will not change, despite IT implementation challenges. However, they highlighted their efforts to ease the burden and cost of implementing the standard and discussed some practical considerations for preparers, as follows:

- No significant changes have been made to the new lease guidance since it was released. The guidance does, however, now include an expedient that allows lessors to combine lease and non-lease components, similar to lessees.
- Common implementation challenges identified by stakeholders include determining completeness of the lease portfolio and identifying embedded leases. Preparers need to perform a thorough review of their existing portfolio and non-lease agreements to ensure all leases, or potential leases, are identified and analyzed.
- Establishing incremental borrowing rates (“IBR”) is a common area of concern during 842 adoption. When establishing IBR, consideration should be given for adjustments based on jurisdictions and collateralization. Companies can start with an unsecured rate, such as intercompany, or observable debt transactions and adjust accordingly.

### ***Riveron Insight***

*As you work through the technical challenges associated with these areas, keep in mind that the new standard is not just an accounting change, but a process change as well. Developing and following the proper internal controls during implementation and post-implementation is integral to the success of applying the new lease standard post-implementation.*

## Non-GAAP Measures

Non-GAAP measures continue to be an area of focus for the SEC. The staff emphasized that investors and creditors expect publicly reported information to be accurate, complete and in compliance with all applicable rules and regulations. Specifically, the staff highlighted two areas of focus: (1) adherence to Compliance and Disclosure Interpretations (“C&DIs”) and (2) the importance of controls and processes when disclosing non-GAAP financial measures.

- The SEC noted the importance of the audit committee’s involvement in the review of non-GAAP financial measures. Audit committees must be comfortable with the information included in SEC filings and how the information is presented.
- The staff clarified and provided examples on how to evaluate whether non-GAAP financial measures involve individually tailored accounting principles. Specifically, the staff noted that non-GAAP measures should either include or exclude certain GAAP amounts, but they should not modify methodology or recognition of an accounting principle.
- The staff acknowledged that changes in the business will lead to changes in non-GAAP measures; however, if there is such a change, registrants should be transparent in their disclosures and explain what changed and why.
- The overall quality of non-GAAP financial measures has improved, specifically the presentation of non-GAAP measures with equal prominence as GAAP measures. In spite of the improvements, the staff noted that preparers should focus on disclosures explaining to investors how they use non-GAAP measures and why those non-GAAP measures are useful to the investors and creditors.

### **Riveron Insight**

*One of the reasons non-GAAP measures garner attention is the lack of transparency in the calculation of these amounts period over period. To ensure consistency in presentation of such non-GAAP measures over time, preparers should have policies addressing how changes in non-GAAP numbers are reported and disclosed.*

## SEC Comment Letter Process

The SEC staff highlighted its perspective that the comment letter process is a dialogue between the registrant and the staff. They reiterated the point that the process may go more smoothly if the registrant asks clarifying questions regarding the staff's comments in order to ensure the registrant is appropriately addressing the matter.

- The staff noted that the registrant should address any considerations regarding materiality early in the comment letter process. If the registrant believes the comment is related to a matter that is immaterial to the company, addressing this concern upfront with the staff is appropriate and will ensure all parties are using their time and resources most effectively.
- The staff offered insight into circumstances where a comment letter is provided to a registrant who is preparing an upcoming filing. If possible, the registrant should address the comment within their existing filing timeline if the comment is relatively minor. However, when the comment is more substantial, requesting more time from the staff to appropriately analyze and consider the response is acceptable, which would result in the comment not being addressed in the upcoming filing.
- The staff also presented their view regarding their practice of providing oral comments. At times, the staff may provide oral comments to the registrant in connection with an ongoing review where a written comment letter has not yet been sent or if there is a time sensitive matter impacting the business, such as relevant current events. If the registrant receives oral comments and believes the staff's question is more than a request for minor clarification, then requesting a follow-up call with all key stakeholders, including accounting and finance leaders and legal counsel, is appropriate. Companies should explain to the staff that a more robust discussion with the individuals who have the requested information would make for a more meaningful discussion.

### **Riveron Insight**

*Consistent with the staff's perspective that the comment letter process is a dialogue, it is appropriate for management to advocate for their disclosure. The staff do not have access to all the information regarding the company that management does. At times, an explanation of the rationale for the disclosure will provide appropriate context and detail to the staff in order to conclude that the current disclosure is appropriate.*

## Cybersecurity & Technology Impact

The staff emphasized the increasing focus on cybersecurity risks, including how those risks are managed and disclosed to the investors. The SEC monitors the news for reports of cyber incidents and may contact affected companies to get a better understanding of the registrant's disclosure of the reported incident.

- The staff noted that if the registrant's business involves handling or managing customer data, they are subject to cybersecurity risk and should consider making relevant disclosures within SEC filings. When preparing those disclosures, management should avoid using boilerplate disclosures. If a data breach has occurred, companies need to ensure their disclosures are updated and provide information about all pertinent facts of the breach.
- The staff highlighted the importance of disclosing how the board of directors oversees cyber risks and the company's controls and procedures around communication and disclosures of the occurrence of such breaches. The staff referenced its earlier statement and interpretive guidance issued on February 21, 2018 to assist public companies in preparing disclosures about cybersecurity risks and incidents.
- Even if the data breach occurred outside of a registrant's financial systems, management and auditors should consider whether such a breach has a negative impact on internal controls over financial reporting (ICFR). If the underlying root cause of the data breach could have impacted the financial system, this would indicate there is a control deficiency in ICFR that would need to be evaluated.

### **Riveron Insight**

*If a company has incurred a data breach and is considering limiting disclosure due to materiality, consideration should be given not just to the data that was extracted as a result of this breach, but to the potential data extraction that could have occurred and whether that changes the materiality conclusion.*

## **Brexit & LIBOR**

SEC Chairman Jay Clayton expressed a view that the impacts of Brexit are being widely underestimated and lacking detail in disclosures. The Chairman indicated that while some companies who may have extensive UK operations have more detailed disclosures, most companies are not disclosing appropriate detail related to how management views the impacts of Brexit on their business.

- The SEC has indicated that Brexit disclosures will be an area of focus in 2019. Companies should review their Brexit disclosures and evaluate if they adequately reflect the impacts of Brexit on their company, rather than boilerplate disclosures that indicate the effects will be unknown.
- After 2021 the banks that submit the rates used to calculate LIBOR will no longer do so; therefore, a transition away from LIBOR is a certainty. The FASB recently issued a standard allowing the Overnight Index Swap ("OIS") rate based on the Secured Overnight Financing Rate ("SOFR") to be designated as a benchmark rate. Additionally, the FASB added a project to its agenda to consider changes to GAAP necessitated by the transition.
- The staff also highlighted a stakeholder consultation on the anticipated impact of the transition from LIBOR on cash flow hedges, including whether LIBOR based interest payments contemplated in the hedge would still be considered probable of occurring and whether the expected transition would impact the assessment of hedge effectiveness. The conclusions reached by the SEC and stakeholder were that there would be no impact on the continued probability of LIBOR based interest payments and that the transition in and of itself would not impact hedge effectiveness. However, an assessment based on individual facts and circumstances should be performed for each such instrument.

### ***Riveron Insight***

*Companies should consider lessons learned related to the Chairman's thoughts on Brexit related disclosures as they consider the shift away from LIBOR. Despite the fact that LIBOR will be available until 2021, companies will likely be impacted earlier as new treasury agreements are finalized utilizing updated benchmarking rates. As such, companies should begin to disclose in more detail how the transition from LIBOR is expected to impact their financial statements.*

## Future Auditing Model

Changes are coming to the auditor report after decades of a standard pass/fail approach. The new auditor reporting model will require the disclosure of critical audit matters (“CAMs”) and be a more informative and subjective report.

- Implementation of the model will occur in phases, with inclusion of CAMs coming in the last phase (years ended after June 30, 2019 for large accelerated filers, and after December 15, 2020 for all other filers). Other changes such as disclosures of auditor tenure and other disclosures around auditor responsibility will be applicable for years ended after December 15, 2017 (this calendar year).
- The PCAOB discussed in detail the expectations around CAMs and noted all of the firms and many companies are doing “dry runs” of auditor reports with CAMs this year. Every audit is expected to identify CAMs which are expected to be substantive and detailed, not boilerplate.

### **Riveron Insight**

*Although current disclosures, including statements of risks and uncertainties required by ASC 275, are not expected to align with CAMs, companies should begin discussions now with their auditors regarding CAMs. This approach will result in fewer surprises and inform thinking around current disclosure, prior to the effective date of the new auditor report.*

## S-X Updates

The staff continues to make strides at simplifying its rules in an effort to facilitate capital formation and improve disclosure effectiveness while protecting investor interest. The SEC provided an overview of the proposed rule aimed at streamlining financial disclosures related to certain registered debt offerings under Regulation S-X Rule 3-10 and Regulation S-X Rule 3-16. They also discussed the progress on various other projects on their near-term agenda.

- The staff is in the process of updating several of the S-X rules, including amendments to S-X Rule 3-05 and Article 11 pro forma financial data. Those amendments will simplify the significance test calculation and include certain pro forma adjustments, such as expected synergies, which may be useful to investors and are currently not allowed by the Article 11 rules.
- The staff highlighted that they are in the process of updating rules to simplify disclosure requirements related to certain registered debt offerings under Regulation S-X Rule 3-10 and Regulation S-X Rule 3-16 and hope to issue those amendments before the end of 2019.

### ***Riveron Insight***

*In advance of the SEC's S-X rule updates currently in process, companies looking for relief from certain disclosure requirements have the ability to request waivers or financial reporting alternatives under Rule 3-13 of Regulation S-X if strict application of Rule 3-05 is burdensome or does not result in presenting valuable information to the investor.*

Additional questions on the conference highlights?

Contact Executive Managing Director, Bill Maloney [HERE](#).



**Prepared remarks by the following speakers at the Conference are available:**

**SEC**

Wesley R. Bricker, chief accountant, Office of the Chief Accountant.  
<https://www.sec.gov/news/speech/speech-bricker-121018-1>

Kevin L. Vaughn, senior associate, Office of the Chief Accountant.  
<https://www.sec.gov/news/speech/speech-vaughn-121018>

Rahim M. Ismail, professional accounting fellow.  
<https://www.sec.gov/news/speech/speech-ismail-121018>

Andrew W. Pidgeon, professional accounting fellow, Office of the Chief Accountant.  
<https://www.sec.gov/news/speech/speech-pidgeon-121018>

Sheri L. York, professional accounting fellow.  
<https://www.sec.gov/news/speech/speech-york-2019-12-10>

Sarah N. Esquivel, associate chief accountant, Office of the Chief Accountant.  
<https://www.sec.gov/news/speech/speech-esquivel-121018>

Emily L. Fitts, professional accounting fellow, Office of the Chief Accountant.  
<https://www.sec.gov/news/speech/speech-fitts-121018>

Tom W. Collens, professional accounting fellow.  
<https://www.sec.gov/news/speech/collens-remarks-2018-aicpa-conference>

**FASB**

Russell G. Golden, chairman.  
[https://www.fasb.org/cs/Satellite?c=FASBContent\\_C&cid=1176171771255&pagename=FASB%2FFASBContent\\_C%2FGeneralContentDisplay](https://www.fasb.org/cs/Satellite?c=FASBContent_C&cid=1176171771255&pagename=FASB%2FFASBContent_C%2FGeneralContentDisplay)

**PCAOB**

George Botic, director, Division of Registration and Inspections.  
<https://pcaobus.org/News/Speech/Pages/botic-protecting-investors-through-change.aspx>

**CAQ**

Cindy Fornelli, executive director.  
<https://www.thecaq.org/center-audit-quality-update-2>

**IASB**

Hans Hoogervorst, chair.  
<https://www.ifrs.org/news-and-events/2018/12/speech-are-we-ready-for-the-next-crisis/>