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AC Insights

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AC Insights provides audit committee members with a summary of financial reporting developments for public companies using IFRS, how those developments might affect your company and things you may want to think about when reviewing financial reports.

In this edition

The year 2018 will require the implementation of two significant accounting standards for many companies – the new standard on revenue recognition and the final standard on financial instruments. In addition to these blockbuster standards, there are a few narrow scope amendments that have become effective. We have outlined these new standards in this edition of *AC Insights*.

During the first quarter of 2018, the IASB finalized its work on the Conceptual Framework, issued an amendment to pension accounting, completed its post implementation review of the fair value measurement standard, and started providing support for its new insurance contracts standard.

The IASB continued its standard setting work on rate regulated activities. The Board continues its research projects on primary financial statements, principles of disclosure, and dynamic risk management. Work is expected to continue on most of these projects into 2019. Certain narrow scope amendments are expected to be completed in the next quarter.

Risks related to marijuana-related business in the US continues to be a focus of the CSA with the recent rescission of the Cole memorandum by the US Federal government. Cybersecurity risks continue to be on the SEC's radar, with new guidance issued on disclosures about cybersecurity risks and incidents in public company disclosures.

On the auditing front, the AICPA has issued some guidance to assist audit committees with their oversight of the disclosure of non-GAAP measures. In addition, the SEC has taken action against certain auditing firms that failed to register with the PCAOB.

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IFRS developments

Standards effective January 1, 2018

The following changes to standards will be effective January 1, 2018 for companies with December 31 year-ends. There may be other standards with a mandatory effective date subsequent to January 1, 2018 that may be adopted earlier, but are not referred to in the table below.

Standard #	Title	Description of change
IFRS 15	*Revenue from contracts with customers*	New comprehensive standard for the recognition, measurement, presentation, and disclosure of revenue and the measurement of certain gains and loss on non-revenue transactions.
IFRS 9	*Financial instruments*	New standard for recognition and measurement of financial instruments, including impairment of financial assets. IFRS 9 has been issued in iterations over several years. The current version is the final full version.
IFRS 7 (Narrow scope amendments)	*Financial instruments – disclosures*	Changes certain disclosures on transition to IFRS 9.
IFRS 4 (Narrow scope amendments)	*Insurance contracts*	Provides options to companies with insurance contracts for the adoption of IFRS 9: *Financial instruments* in conjunction with the new standard on insurance contracts, IFRS 17 which is effective in 2021.
IFRS 2 (Narrow scope amendments)	*Share-based payment*	Clarifies the measurement basis for cash-settled awards and the accounting for modifications to such awards. Also, provides an exception to the liability classification of awards with cash payments for tax withholdings.
IAS 28 (Annual improvements)	*Investments in associates and joint ventures*	Clarifies the use of the election by venture capital entities, mutual funds, unit trusts and other similar entities to measure investments at fair value through profit or loss.
IAS 40 (Narrow scope amendments)	*Investment property*	Clarifies that a transfer to, or from, investment property, occurs only when there has been a change in use of the property.
IFRIC 22	*Foreign currency transactions and advance consideration*	Clarifies that a foreign currency denominated transaction is measured at the exchange rate when the non-monetary item is initially recognized and not the date any advances are made related to those transactions.

Clarification of accounting for defined benefit plan amendments, curtailments and settlements

In February 2018, narrow scope amendments were made to IAS 19: *Employee benefits* to clarify the accounting when there are amendments, curtailments or settlements of employee defined benefit plans.

After a plan amendment, curtailment, or settlement of an employee defined benefit plan, entities are required to update their actuarial assumptions to determine the past service cost or a gain or loss on settlement. Any past service cost and gain or loss on settlement, after remeasurement of the net defined benefit liability and plan assets before and after these changes, is recognized in profit or loss for the period of the amendment, curtailment or settlement.

The IFRS amendment clarifies that the updated assumptions are also to be used to determine current service cost and net interest expense for the remainder of the annual period. Previously, the current service cost and net interest expense were only updated annually at the start of the financial year.

A plan amendment, curtailment or settlement might reduce or eliminate a surplus, which may have been subject to the asset ceiling test. Any past service cost, gain or loss resulting from these changes to the plan is determined without considering the asset ceiling test. The impact on any prior asset ceiling test is recognized in other comprehensive income and is not reclassified to profit or loss because of these changes.

The amendments are applied prospectively to plan amendments, settlements or curtailments that occur after the beginning of the first annual reporting period beginning on or after 1 January 2019.

Fair value measurements standard working as intended

In January 2018, the results of the Post-Implementation Review of IFRS 13: *Fair value measurement* (PIR) was tabled with the IASB. The results were summarized from 67 comment letters received on the Request for Information (RFI) on the PIR and 24 meetings with stakeholders.

The key message from the IASB staff summarizing the findings from the PIR is that "IFRS 13 works well and has achieved its objectives". The IASB has accepted this conclusion.

The RFI has several areas of focus, with the following findings:

- There was a general consensus that ***disclosures on Level 3 fair value measurements*** were useful; however, concerns were raised about the utility of quantitative sensitivity analysis and certain reconciliations. The most useful disclosures about Level 3 fair values were those about valuation techniques and inputs, quantitative significant unobservable inputs, and the fair value hierarchy. Concerns were raised about the effect of aggregation and the use of a tick-box approach to the disclosures, which may result in the disclosure of immaterial information.

- Users, regulators, preparers, auditors, and national standards setters, all voiced concerns over the lack of resolution of the ***PXQ issue***. The PXQ issue relates to whether investments with quoted market values should be measured based simply on the quoted market value multiplied by the number of units held or be adjusted for other factors. While users support no adjustments to the quoted market price, others stated the measurements should consider the investment as a whole and adjust for the value of control, the value of synergies, and market liquidity, as applicable.

- Many respondents indicated they found the application of the principle of the ***highest and best use of non-financial assets*** challenging, in particular considering whether the alternative use was legally permissible. However, others indicated that the current use is generally the highest and best use and an alternative use is rare.

- Respondents indicated that the ***application of judgment*** was challenging in areas such as assessing whether (a) a market is active, and (b) an unobservable input is significant to the determination of a fair value. These respondents asked the IASB for more guidance on these assessments.

- A small subset of respondents commented on the ***fair value measurement of unquoted equity instrument***. Those respondents asked for more guidance in areas such as the valuation of early stage entities, determination of the cost of capital, determination of premiums and discounts, and the impact of restrictions.

The IASB considered these findings at its March 2018 meeting and decided to use the findings in its current project on Better Communications in Financial Reporting dealing with primary financial statements and principles of disclosure. The IASB will also continue liaison on these matters with the valuation profession. The IASB decided there were no specific changes currently required on IFRS 13.

Implementing the new standard on insurance contracts

To assist the accounting community with the implementation of IFRS 17: *Insurance contracts*, the IASB established a Transition Resource Group (TRG). The TRG held its first meeting in February 2018.

The role of the TRG is to provide implementation support as industry experts. The TRG does not make any decisions, but may recommend certain matters to the IASB based on new and relevant information obtained during the implementation process. The TRG acknowledged that the implementation of IFRS 17 would involve operational burden and additional costs for insurers.

As of January 23, 2018, 27 submissions were received by the IASB, of which 13 were disposed as either being addressed in IFRS 17, not meeting the submission criteria, or being tabled for the IFRS maintenance process. On four issues raised, the IASB staff has requested further information from the submitter.

At the February meeting, the TRG grouped the remaining issues into the following topics:

- The separation of insurance components in a single insurance contract;
- The boundary of contracts with annual repricing mechanisms;
- The boundary of reinsurance contracts held;
- The insurance cash flows paid and future renewals;
- The determination of the quantity of benefits for identifying coverage units; and
- The insurance acquisition cash flows when using the fair value transition.

Implementation guidance was provided on these topics; however, the TRG asked the IASB staff to bring further information on the determination of the quantity of benefit for identifying coverage units. The TRG did not refer any matters to the IASB for further consideration. The next TRG meeting is in May 2018.

For more information, please ask for the summary of the discussion of the February 2018 TRG meeting.

Conceptual framework updated

In March 2018, the IASB issued its revised *Conceptual Framework to Financial Reporting* (CF), which describes the objectives and concepts for general purpose financial reporting. The revised framework builds on the existing framework by updating it to reflect the current environment, improving and clarifying some guidance, and filling in the gaps by addressing important issues not previously addressed.

The CF is not a standard and does not override any specific guidance in any IFRSs. The framework is a tool to assist the IASB in developing IFRSs on a consistent basis, to assist preparers to develop accounting policies when there is no applicable IFRSs to address their situation, and to assist all parties in understanding and interpreting IFRSs.

What's new?

The revised CF addresses certain topics that were not previously included in the CF. The following changes reflect additions to the CF.

- The concept of a ***reporting entity*** was added. A reporting entity is simply an entity that chooses to prepare financial statements. The concept is fairly flexible, but the boundaries of a reporting entity are determined by considering the information needs of users. The reporting entity does not have to be a legal entity; it could be a portion of an entity or consist of more than one entity. However, a reporting entity would not comprise an arbitrary or incomplete collection of assets, liabilities, equity, income and expenses.

- The new chapter on ***measurement*** continues to permit different measurement bases (i.e., historical cost, fair value, value in use or fulfilment value, and current cost) for different assets, liabilities and other elements, with the possibility of more than one measurement basis for components of a transaction. The CF now includes various factors for selecting a measurement basis. These factors are consistent with the qualitative characteristics of financial information – relevance and faithful representation, as well as the consideration of cost constraints in measuring an item.

- The CF includes a new chapter on ***presentation and disclosure*** describing how information should be presented and disclosed to achieve effective communication. The statement of profit or loss is described as the primary source for financial performance information**.** The CF also acknowledges the concept of other comprehensive income (OCI) and states that decisions of which elements or components are included in OCI should be decided during the standard setting process.

- New guidance on ***derecognition of assets and liabilities*** addresses when assets and liabilities are removed from the statement of financial position. Assets are normally removed when an entity loses control of all or part of the recognized asset. Liabilities are normally removed when an entity no longer has a present obligation for all or part of the recognized liability. In certain limited cases, it may be necessary to continue to recognize a transferred component of an asset or a liability along with a liability or asset for any proceeds received or paid.

What's been updated?

The definitions of all elements for financial statements, except for equity, have been refined and updated. The updates include the following:

- Revision of the ***definition of an asset*** by (1) clarifying that an asset is an economic resource and not the ultimate inflow of economic benefits; (2) deleting the notion of "expected flow" as the flow does not need to be certain or even likely for economic benefits to arise; and (3) stating that a low probability of economic benefits affects

whether the asset is recognized and how it is measured.

- Revision of the ***definition of a liability*** with the same clarification about economic resources and deletion of "expected flow" as for the definition of an asset (see (1) and (2) above). In addition, the definition of a liability introduces the "no practical ability to avoid" criterion. The CF clarifies that the "no practical ability to avoid" criterion goes beyond contractual requirements and may arise from (1) an entity's customary practices, policies and statements, or (2) if the duty or responsibility is conditional on a particular future action by the entity itself, an inability to avoid taking that action.

- The addition of a definition of an ***executory contract*** as a right and an obligation to exchange economic resources, which cannot be separated. The combined right and obligation represents a single asset if the terms are favourable or a single liability if the terms are unfavourable.

- Replacement of the existing criteria for ***recognizing assets and liabilities*** (and related income, expenses or changes in equity) with criteria that refer explicitly to the qualitative characteristics of useful information. Assets and liabilities are recognized when:

  – There is relevant information about the asset, liability or other elements (the relevance may be affected by low probability of a flow of economic benefits or uncertainty about the existence of the asset or liability); and

  – The recognition results in a faithful representation of the asset, liability or other elements (faithful representation may be affected by measurement uncertainty, accounting mismatches, and presentation and disclosure requirements).

What's been clarified?

The Board did not fundamentally reconsider the objectives of financial reporting or the qualitative characteristics of useful financial information. Certain clarifications were made to these sections, including:

- Giving more prominence to ***management accountability or stewardship*** of an entity's resources as an objective of general purpose financial reporting.

- ***Bringing back prudence*** as a qualitative characteristic of useful financial information. Prudence means the exercise of caution when making judgments under conditions of uncertainty. Prudence does not allow for overstatement or understatement of assets, liabilities, income or expenses.

- Explicitly incorporating the concept of ***substance over form*** within the description of the qualitative characteristic of faithful representation.

- Explaining that ***measurement uncertainty*** does not prevent information from being useful; however, in some cases information that has a lower measurement uncertainty, even though less relevant, may provide more useful information.

When is the revised CF effective?

The revised CF will be used in the IASB and IFRIC standard setting processes immediately. Preparers who develop accounting policies based on the CF would use the revised CF for annual periods beginning on or after January 1, 2020.

The revised CF will be beneficial to ensure IFRSs are conceptually consistent and that similar transactions are treated the same way. Any inconsistencies between existing IFRSs and the revised CF will continue to exist until the IASB redevelops those IFRSs or make improvements to those IFRSs.

CSA developments

CSA plans to reduce regulatory burden

In March 2018, the CSA published an update to the CSA Consultation Paper 51-404: *Considerations for Reducing Regulatory Burden for Non-Investment Fund Reporting Issuers,* which was published in April 2017. The purpose of the Paper was to identify and consider areas of securities regulation that could be improved by reducing regulatory burden, while still providing investor protection and the efficiency of the capital markets. Based on the feedback received from stakeholders, the CSA has initiated six projects to make changes to the regulatory regime. There is no assurance that changes will ultimately be adopted because of these projects.

The six projects are:

- Potential alternative prospectus model that is more concise and focused than the current short form prospectus model.
- Facilitating at-the-market (ATM) offerings by providing exemptive relief from or eliminating shelf prospectus requirements and conditions.
- Reconsideration of the historical financial statements required for the primary business in an initial public offering.
- Business acquisition reporting by either removing or modifying requirements.
- Revisiting continuous disclosure requirements, which may consider eliminating disclosures that are duplicative among the financial statements, MD&A, and other requirements; consolidating annual disclosures into one reporting document; and reducing the volume of information required in annual and interim filings to improve the quality and accessibility of the information. This will be a longer-term project.
- Enhancing electronic delivery of documents to investors.

The CSA will use their normal processes for developing amendments to the securities legislation, rules and instruments.

US marijuana views

The CSA has revised its guidance on disclosure expectations for specific risks facing issuers with marijuana-related activities in the US. These views are based on the fact the cultivation, distribution and use of marijuana is illegal under US federal laws. We reported on the original guidance in our winter 2018 edition of *AC Insights*. The revised guidance is included in CSA Staff Notice 51-352 (Revised): *Issuers with US marijuana-related activities.*

Background

In 2013, the US federal government allowed states to legalize marijuana activities if certain criteria were met, which were set out in a Department of Justice memo, referred to as the Cole memorandum. In January 2018, the US Attorney General Jeff Sessions rescinded the Cole memo. This rescission allows federal prosecutors to decide individually how to apply the federal law. This change in policy could increase risks for companies that are operating in states that have legalized marijuana for medical and/or recreational purposes.

Disclosures of enforcement risk

The CSA Staff Notice provides the staff's specific disclosure expectations for issuers with US based marijuana activities. The extent of disclosures will

depend on the nature of the issuer's activities, which may include (a) the cultivation and distribution of marijuana under a state license; (b) a non-controlling investment in a US marijuana-related business; or (c) provision of goods or services (financing, branding, recipes, leasing, consulting and administrative services) to US marijuana-related businesses.

All issuers with US marijuana-related activities are required to:

- Disclose the nature of their involvement;
- State that marijuana is illegal under US federal law and enforcement of the laws is a significant risk;
- Disclose the current US position on enforcement;
- Disclose risks of suspension or withdrawal of services or financing by third parties and regulatory restrictions;
- Quantify the balance sheet and operating statement exposure to US marijuana activities; and
- Disclose any legal advice obtained on compliance with regulatory frameworks and potential exposure to US federal law.

For issuers with a controlling or non-controlling interest in such businesses, information should be provided on state regulations and the issuer's compliance with the state licensing requirements and regulatory framework. For issuers with ancillary association with US marijuana-related activities, the issuer should comment on the customer's or investee's compliance with state licensing requirements and regulatory framework.

These disclosures should be updated when a government policy changes or there are legislative amendments on marijuana sales and use in the US.

Failure to make appropriate disclosures could result in non-receipt of prospectuses, restatement of disclosures, or referral to enforcement.

The CSA will continue to monitor industry developments and consider whether further regulatory action is required.

SEC developments

Cybersecurity disclosures for investors

The SEC issued interpretative guidance in February 2018 to assist public companies in preparing their disclosures about cybersecurity risks and incidents. The guidance is based on existing reporting requirements and addresses the importance of cybersecurity policies and procedures.

In the statement from the SEC Chair, Jay Clayton stated, “cybersecurity is critical to the operations of companies and our markets.” He requested public companies to stay focused on these issues and take required action to inform investors about material cybersecurity risks and incidents on a timely basis.

The interpretative release (1) stresses the importance of establishing and maintaining comprehensive policies and procedures related to cybersecurity risks and incidents; and (2) reminds companies and their insiders about insider trading and use of selective disclosures when cybersecurity risks or incidents occur.

Policies and procedures

Companies are encouraged to adopt comprehensive policies and procedures for cybersecurity and assess the company’s compliance regularly, including their disclosure controls to ensure there is timely reporting of risks and incidents. The controls and procedures should enable companies to identify the risks and incidents, assess and analyze their impact, evaluate their significance, involve the appropriate personnel with expertise in the area, and make timely disclosures as appropriate.

Disclosures

In assessing the materiality of disclosures about cybersecurity risks and incidents, the SEC indicates that companies need to assess the importance of the compromised information and its impact on company operations. Companies should consider the range, nature, extent and potential magnitude of the harm such incidents could cause. Harm may result to the company’s reputation, financial performance, customer and vendor relationships, or results in litigation or regulatory actions.

The SEC does not expect detailed disclosures of a company’s security plan and understands that information about incidents may evolve. The information is expected to be tailored to each company’s particular risks and incidents and companies are discouraged from making generic cybersecurity related disclosures.

SEC disclosure requirements for annual reports on Form 10-K or 20-F require companies to disclose risk factors. In evaluating disclosure of cybersecurity risks, companies should considered the severity and frequency of past cybersecurity incidents, the probability and magnitude of potential incidents, the adequacy of the company’s preventative actions, company specific risks that may heighten cybersecurity risks, costs of maintaining cybersecurity protections, potential of reputational harm, and other consequences of a cybersecurity breach.

MD&A disclosures may be required considering the cost of ongoing cybersecurity efforts and the costs and consequences of cybersecurity incidents. The description of a business may warrant disclosure about cybersecurity matters if cybersecurity incidents or risks materially affect a company’s products, services, relationships, or competitive conditions. Any material legal proceedings from a cybersecurity incident would require disclosure in the annual report. Disclosures about a board’s oversight of risk management may also need to consider cybersecurity when such risks are material.

More information

Further information on the SEC guidance can be found in SEC Release Nos. 33-10459 and 34-82746: *Commission Statement and Guidance on public company cybersecurity disclosures.*

Auditing developments

AICPA roadmap on non-GAAP measures

The AICPA issued a publication in March 2018 to provide a set of considerations for audit committees on non-GAAP measures presented by companies. The publication: ***Non-GAAP measures: A roadmap for audit committees*** was released with a companion video featuring interviews with audit committee chairs on their experiences in overseeing non-GAAP measures.

The objective of the publication is to support audit committees in carrying out their oversight of non-GAAP measures and achieve more transparency, consistency, and understanding of non-GAAP measures.

In addition to presenting the current environment surrounding the preparation, presentation and oversight of non-GAAP measures, the AICPA has provided audit committees with guidance on assessing non-GAAP measures including:

- Topics of discussion between management and the audit committee on the non-GAAP measures to be presented;
- Understanding the auditor's role regarding non-GAAP measures; and
- Best practices that can be applied to support the presentation of non-GAAP measures.

Copies of the publication can be obtained from the Center for Audit Quality of the American Institute of Certified Public Accountants.

Improvements in Canadian audits encouraging

CPAB's report on its findings of its 2017 inspections was released in March 2018. CPAB inspected 128 annual audit files of 14 audit firms during 2017. CPAB was encourage by the decreasing trend in significant findings, but found that audit quality remains inconsistent, indicating firms need to review their approach to audit quality and enhance their focus on consistent execution across the respective firm.

Significant findings were made in 15 files in 2017 compared to 24 in 2016. The majority of these significant findings required audit firms to carry out additional procedures to determine the need, if any, for a restatement of the client's financial statements due to material error. Three restatements resulted from these additional procedures.

Firm level quality management seen as the key to improvements

CPAB believes that higher quality audits are achievable when "the right people, policies and procedures are in place." CPAB has begun to focus on firm level quality management systems and processes of the Big Four firms. CPAB will focus on the accountability for audit quality within the firm; the management of client and audit risk; the management of people from partners to all levels of staff including industry and other specialists as well as the allocation of the right people to each audit; and the oversight of audits by the firm leadership.

Performance across all firms improving

For the Big Four firms (Deloitte, EY, KPMG and PwC), CPAB found that each firm demonstrated an acceptable level of inspection findings overall, but there was a need to embed audit approach improvements into every practice and every engagement. Out of the 86 engagement files inspected, 6 had significant findings resulting in two restatements.

Twenty engagement files of other national / network firms (BDO, Grant Thornton, MNP and Raymond Chabot Grant Thornton) were inspected resulting in 6 with significant findings, but no restatements. CPAB found significant

improvements in three of these firms, but noted one firm continues to experience challenges.

Six large regional firms were inspected resulting in 3 significant findings and one restatement out of the 19 engagement files examined. The number of significant findings decreased from the prior year indicating firms had undertaken targeted improvement to resolve recurring issues; however CPAB continues to identify potential weaknesses in the quality control systems of these firms.

Some common issues continue to be challenging for auditors

CPAB outlined in their report certain common issues that continue to challenge auditors. Areas requiring improvements related to (1) the execution of basic audit procedures; (2) the use of professional judgment and scepticism in assessing the appropriate of audit tests and the reasonableness of evidence provided by management; and (3) the auditing of significant accounting estimates, particularly the appropriateness and consistency of management's financial inputs.

The report provides several questions that the audit committee could ask of the auditors to understand the quality of the audit, including the quality management systems and processes at the audit firm.

Under the CPAB Protocol with PwC, a copy of this report will be provided to audit committees.

CPAB supports Audit Quality Indicators

In 2016, CPAB launched an Audit Quality Indicators (AQIs) Pilot project with Canadian audit committees to obtain feedback about the usefulness of AQIs and to encourage innovation in the use of AQIs. In November 2017, CPAB held a roundtable with audit committee chairs, management and lead audit partners of the participants in the project. CPAB's 2017 Interim Update was issued in March 2018.

The Update outlined five key themes of the Roundtable:

- Growing support for management related AQIs measuring management's project management, the quality of management control systems, or the timeliness of management's remediation of control deficiencies.
- Upfront discussions among management, the auditor and the audit committee about AQIs provide the most value by developing an understanding of audit quality, expectations around audit quality and the coordination of the various parties efforts.
- The selection of AQIs should be limited to 10 or less (with the average number selected by participants in the project being eight). The selection of AQIs should be well thought out and consider the cost-benefit of each.
- Need for continual review of the AQIs selected to ensure they require changes at the audit firm, the business environment, audit risks, and the needs of the audit committee.
- Development of objective benchmarks to evaluate AQIs is challenging, and development of acceptable ranges or directional trends may be an alternative to consider.
- There are diverse opinions on the usefulness of specific AQIs depending on the unique needs and circumstances on individual audit committees.

The update outlined that strong project management was key to audit quality and many participants selected project management type AQIs. In addition, the following AQIs are frequently used by participants:

- Timing of audit execution;
- Use of specialists;
- Partner / manager leverage;

- Experience of engagement team;
- Management deliverable; and
- Number of hours spent of key risk.

CPAB will be wrapping up the project in 2018 with one final feedback and will publish a summary of their findings from the project. CPAB will continue to promote AQIs and plans to:

- Work with CPA Canada and the Institute of Corporate Directors to develop an AQI Guide to assist audit committees in implementing AQIs for the first time; and

- Launch an AQI Network to share information among and provide support to current and future AQI users.

Tips for audit committees of financial institutions

On December 13, 2017, CPAB held its annual Financial Institutions Industry Forum for audit committee chairs of large Canadian banks and insurance companies. The Forum covered emerging and topical developments for audit committees of these institutions.

The following matters were addressed at the forum:

- Technology risk relating to industry innovation, transformation, implementation of systems, and cybersecurity; the need to have sound strategies dealing with these risks; the scope of the board's oversight over technology partnerships and joint ventures with third parties; and plans to respond to crisis and other unforeseen events.

- The new auditor reporting requirements under Canadian Auditing Standards and the PCAOB standards, the differences in the reporting models, and concerns of disclosure of proprietary or sensitive information in key audit matters section of the reports.

- Implementation challenges of new standards that will become effective for financial institutions in the upcoming year.

- The efficiency and effectiveness of the audit committees, including efforts to streamline information provided to audit committees, use of pre- and post-meetings with the chair to direct management and the auditors on matters of focus for meetings and communications with the committee, and the use of consent agendas to deal with routine matters.

- Tools and activities to enhance the oversight of the financial reporting process and the audit including audit quality indicators and comprehensive reviews of the auditor's performance.

CPAB holds similar forums with other industry groups to foster an open dialogue on improving audit quality and the oversight of auditors.

Improper foreign audits result in fines and loss of profits

In March 2018, the SEC charged the principal auditors of two SEC registrants with improperly relying on the work of two foreign component auditors that were not registered with the PCAOB. The foreign component auditors had audited the majority of the assets and revenues of the publicly traded companies. The SEC claims that the principal auditors had failed to consider the registration status of the firms that did the majority of the audit work.

The SEC found that (1) the foreign component auditors had violated the Sarbanes-Oxley Act because they were not registered with the PCAOB; and (2) the principal auditors had engaged in improper professional conduct, violated the auditing requirements of Regulation S-X, and caused their audit client to violate their reporting requirements.

Without admitting or denying the charges, the principal auditors agreed to pay significant fines and the secondary auditors agreed to disgorge the profits from their audits as well as interest.

The key message of this SEC action is that it is important that all auditors substantially involved in the audit of a SEC registrant be properly registered with PCAOB to allow the PCAOB to exercise its oversight responsibilities.

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