

# *The US Regulatory Environment: 2013 and Beyond*

January 28, 2013

Wayne Carnall  
Partner

# SEC leadership

## Commissioners



Elisse Walter (D)  
Chairman<sup>(1)</sup>



Daniel Gallagher (R)



Luis Aguilar (D)



Troy Paredes (R)

Vacant position

## Office of the Chief Accountant

### Paul Beswick, Chief Accountant

Julie Erhardt, Deputy Chief Accountant – International  
Brian Croteau, Deputy Chief Accountant – Professional Practice

## Division of Corporation Finance

### Lona Nallengara Acting Director

Craig Olinger, Acting Chief Accountant

## Division of Enforcement

### Open Director

Howard Scheck, Chief Accountant

(1) On December 14, 2012 Elisse Walter was appointed Chairman after Mary Shapiro resigned from the SEC

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## ***Mary Jo White – New Chairman***



- Former US Attorney for the Southern District of New York
- Private practice – Debevoise & Plimpton
- Expectations

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# ***SEC***

- Impact of election
- Changes in Senior Staff
- Dodd-Frank Act - volume of rules
- Use of SEC disclosure system to implement social change
  - Conflict Minerals
  - Office of Global Security Risk
- Challenges to rules based on cost/benefit analysis
- Jobs Act

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# ***IFRS in the United States***

- **DEVELOPMENTS IN THE PAST – Up to 2010**
  - Historical perspective
  - Roadmap and limited option– 2008
  - Work Plan for Global Accounting Standards – 2010
- **DEVELOPMENTS IN 2011**
  - Staff Paper - *Exploring a Possible Method of Incorporation*
  - Staff Paper - *A Comparison of US GAAP and IFRS*
  - Staff Paper - *An Analysis of IFRS in Practice*
  - FAF/FASB Paper
- **DEVELOPMENTS IN 2012 AND BEYOND**
  - Completion of Work Plan
  - Report of the Trustees of the IFRS Foundation
  - Next steps????

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## ***Consistency in the Application of IFRS***

*Companies will read IAS with their own national bias. Given a transaction, the people in the U.K. could determine that the accounting is the same under IAS as U.K. GAAP, and the people in Mexico could determine there is no difference between Mexican GAAP and IAS. Both believe the accounting complies with IAS, but they will account for the transaction differently.*

*Wayne Carnall*

CFO Magazine

January 1997

# ***SEC structure***

<b>Office of the Chief Accountant ("OCA")</b>	<b>Division of Corporation Finance ("Corp Fin")</b>	<b>Division of Enforcement</b>
<ul style="list-style-type: none"><li>• Interacts with standard setters:<ul style="list-style-type: none"><li>- FASB</li><li>- IASB</li><li>- PCAOB</li></ul></li><li>• Considers Company positions on accounting, financial reporting and auditing matters, particularly unusual, complex or innovative transactions</li></ul>	<ul style="list-style-type: none"><li>• Ensures compliance in form and content<ul style="list-style-type: none"><li>- Quarterly &amp; annual reports</li><li>- Registration statements</li><li>- Transactional filings</li></ul></li><li>• Considers registrant requests for waivers and interpretations of form and content</li><li>• Each registrant is reviewed at least once every three years<ul style="list-style-type: none"><li>- Comment letter may be issued based on review</li><li>- May refer to Enforcement</li></ul></li></ul>	<ul style="list-style-type: none"><li>• Investigates possible federal securities law violations<ul style="list-style-type: none"><li>- Misrepresentation or omission of important information about securities</li><li>- Manipulating the market prices of securities</li><li>- Insider trading</li><li>- Selling unregistered securities</li></ul></li></ul>

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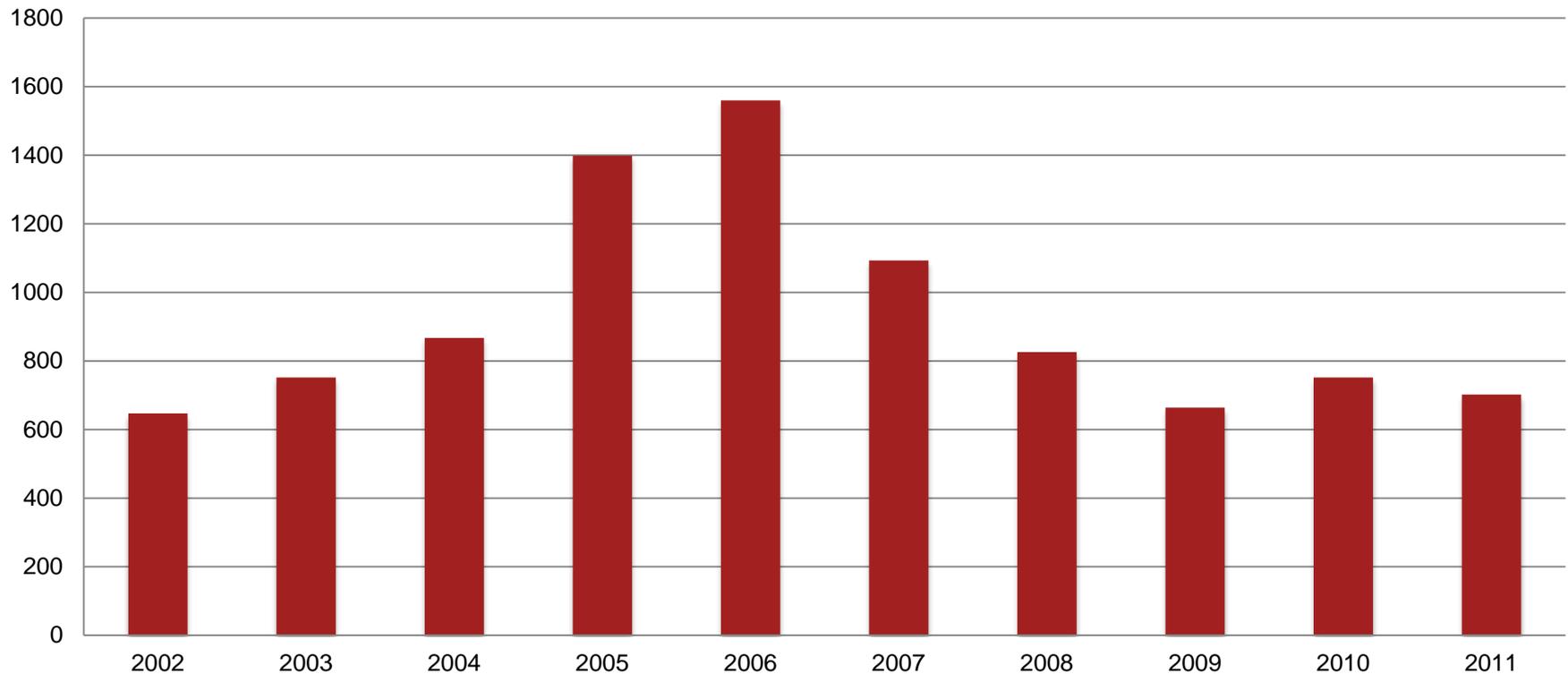
## ***Division of Enforcement***

- Whistleblower
- Materiality
- China
- Estimates
- FCPA – Joint paper issued with DOJ
- BP
- Netflix – Wells Notice
- Other

# ***Restatement trends***

10 year comparison (Source: Audit Analytics)

## **Total restatements per unique filer**



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## ***Restatement trends***

(Source: Audit analytics)

1. Debt, quasi-debt, warrants & equity (BCF)
2. Expenses (payroll, SGA, other)
3. Cash flow statement
4. Acquisitions, mergers, disposals and reorganization accounting issues
5. Revenue recognition
6. Tax expense, benefit, deferral and other issues
7. Liabilities, payables, reserves, and accrual estimates
8. Accounts/loans receivables, investments & cash issues
9. Deferred, stock-based, and/or executive compensation
10. Intangible or fixed asset issues

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## ***The SEC & Valuation Professionals***

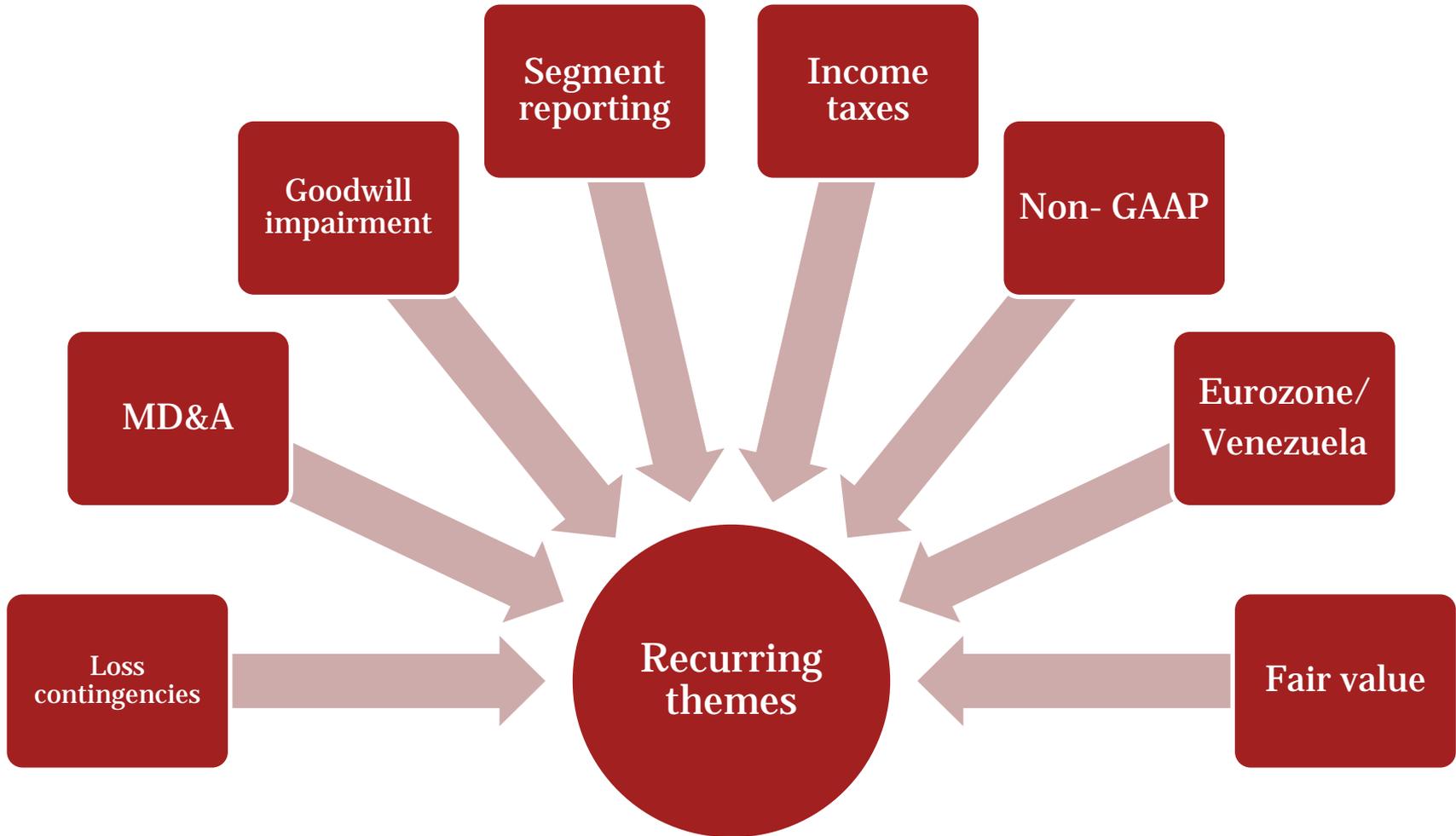
- Office of the Chief Accountant
- Division of Corporation Finance
- What do they do?
- Has their work ever led to a restatement?

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## ***Importance of valuation professionals working with the auditor***

- Purchase price allocation
- Goodwill impairment
- Cheap stock
- Impairment of equity investments
- Deferred tax valuation allowance
- Valuation of own credit
- Liquidity adjustments
- Other

# ***SEC comment letter trends***



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## ***Fair Value***

- SEC has challenged registrants that don't provide quantitative information for unobservable inputs.
- Disclose weighted average of significant inputs when the range is wide.
- Looking for expanded disclosures about valuation techniques for "Level 2" fair value measurements.
- Looking for greater granularity around the qualitative disclosures.

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## ***Sample SEC comments – Fair value***

“We acknowledge your disclosures added under the new requirements of ASU 2011-04. Please provide us proposed revised disclosure to be included in future periodic reports that addresses the following comments:

- Discuss the interrelationships between the unobservable inputs identified in the table on page XX and how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement as stipulated in ASC 820-10-50-2g;
- Discuss the valuation techniques used to measure Level 3 assets and liabilities disclosed at fair value but not reported at fair value as presented in the table on page XX and as required by ASC 820-10-50-2E. In this regard, for example, it appears that your general disclosure of techniques used to value investments held to maturity on page XX discusses the use of observable inputs but not unobservable inputs.”

“We note that you disclose the significant unobservable inputs used in your Level 3 fair value measurements in addition to the range of such inputs. Given the wide range of inputs in certain cases, please revise your disclosure in future filings to also disclose the weighted average of the significant unobservable inputs reported. Refer to the illustration provided in ASC 820-10-55-103.”

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## ***Dear CFO Letters***

- **March 2008 – Disclosures regarding application of SFAS 157 – Fair value measurements**
- **September 2008 – Disclosures regarding application of SFAS 157**
- **August 2009 - MDA disclosure regarding loan loss**

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## ***Loans Measured for Impairment Based on Collateral Value CF Disclosure Guidance 5***

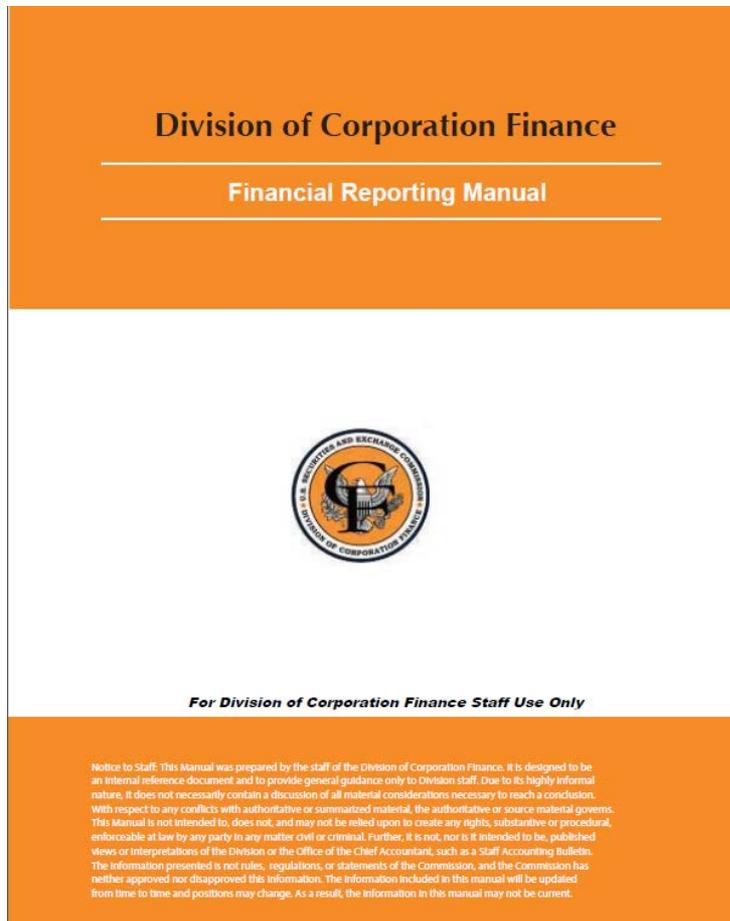
- How and when they obtain third-party appraisals
- The types of appraisals they obtain, such as “retail” value or “as-is” value
- What procedures they perform between receiving updated appraisals to ensure that they appropriately measure loan impairments
- If applicable, the reasons they do not obtain appraisals in a timely manner
- The reasons they make any adjustments to appraised values when calculating impairment
- What procedures they perform to estimate the fair value of the collateral when they do not use external appraisals or have not obtained updated appraisals.

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## ***102(e) Proceeding against KPMG Partner & Mgr January 2013***

- TierOne Corporation
- Valuation of collateral supporting loan values
- Use of appraisals
- Adjustments to appraisals

# *The Financial Reporting Manual*



- Document prepared by the Division of Corporation Finance – interpretive guidance on various reporting and disclosure issues
- Updated quarterly and posted on SEC’s website

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## ***Cheap Stock – FRM 7520***

In the evaluation of the assumptions used in and the results of applying an appropriate valuation methodology to estimate the fair value of the stock, the registrant should consider the proximity of the issuance to the offering, intervening events, transfer restrictions and exercise dates, and profitability and financial condition of the company at the date of the valuation. If the estimated fair value of the stock is substantially below the IPO price, the registrant should be able to reconcile the difference between them (for example, explain the events or factors that support the difference in values). The reliability of a valuation specialist's fair value determination may be affected by the timing of the valuation (contemporaneous versus retrospective) and the objectivity of the specialist (unrelated versus related-party).

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## ***Stock Compensation in IPOs***

### ***MD&A Disclosure – FRM 9520***

- Description of methods and assumptions – used to determine fair value
- Table – information about the instruments granted during the 12 months preceding the most recent balance sheet
- Explanation of changes in fair values
- Updated disclosures after the most recent balance sheet – including prices that are materially different from estimated IPO price

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# ***Goodwill Impairment – Disclosure***

## ***FRM 9510***

- The percentage by which fair value exceeded carrying value as of the date of the most recent test;
- The amount of goodwill allocated to the reporting unit;
- A description of the methods and key assumptions used and how the key assumptions were determined;
- A discussion of the degree of uncertainty associated with the key assumptions. The discussion regarding uncertainty should provide specifics to the extent possible (e.g., the valuation model assumes recovery from a business downturn within a defined period of time); and
- A description of potential events and/or changes in circumstances that could reasonably be expected to negatively affect the key assumptions.

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## ***Consents from Third Party Valuation Experts***

- What is the significance of a consent?
- CDI - Securities Act Rules 233.02
- Disclosure in the filing – what triggers the need for a consent
  - Level of responsibility by the company

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## ***Compliance Disclosure & Interpretations (CDI) Securities Act Rules – 233.02***

**Question:** A registrant has engaged a third party expert to assist in determining the fair values of certain assets or liabilities disclosed in the registrant's Securities Act registration statement. **Must the registrant disclose in the registration statement that it used a third party expert for this purpose?** In what circumstances must the registrant disclose the name of the third party expert in its registration statement and obtain the third party's consent to be named?

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## ***Compliance Disclosure & Interpretations (CDI)*** ***Securities Act Rules – 233.02***

**Answer:** The registrant has no requirement to make reference to a third party expert simply because the registrant used or relied on the third party expert's report or valuation or opinion in connection with the preparation of a Securities Act registration statement. The consent requirement in Securities Act Section 7(a) applies only when a report, valuation or opinion of an expert is included or summarized in the registration statement and attributed to the third party and thus becomes "expertised" disclosure for purposes of Securities Act Section 11(a), with resultant Section 11 liability for the expert and a reduction in the due diligence defense burden of proof for other Section 11 defendants with respect to such disclosure, as provided in Securities Act Section 11(b). figures are attributed to the registrant.

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## ***Compliance Disclosure & Interpretations (CDI)***

### ***Securities Act Rules – 233.02 - Cont***

If the registrant determines to make reference to a third party expert, the disclosure should make clear whether any related statement included or incorporated in a registration statement is a statement of the third party expert or a statement of the registrant. If the disclosure attributes a statement to a third party expert, the registrant must comply with the requirements of Securities Act Rule 436 with respect to such statement. For example, if a registrant discloses purchase price allocation figures in the notes to its financial statements and discloses that these figures were taken from or prepared based on the report of a third party expert, or provides similar disclosure that attributes the purchase price allocation figures to the third party expert and not the registrant, then the registrant should comply with Rule 436 with respect to the purchase price allocation figures. On the other hand, if the disclosure states that management or the board prepared the purchase price allocations and in doing so considered or relied in part upon a report of a third party expert, or provides similar disclosure that attributes the purchase price allocation figures to the registrant and not the third party expert, then there would be no requirement to comply with Rule 436 with respect to the purchase price allocation figures as the purchase price allocation

# ***PCAOB leadership***

## **PCAOB board members**



**James R. Doty**  
Chairman



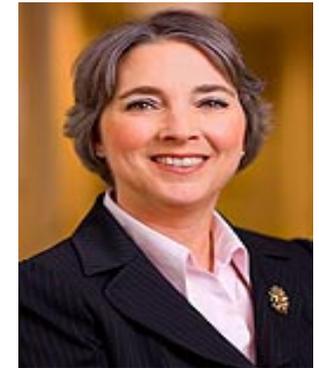
**Jay D. Hanson**



**Lewis H. Ferguson**



**Steven B. Harris**



**Jeanette M. Franzel**

## **Office of the Chief Auditor**

**Martin F. Baumann, Chief Auditor & Director of Professional Standards**  
**Jennifer A. Rand, Deputy Chief Auditor/Deputy Division Director**  
**Greg Scates, Deputy Chief Auditor**  
**Keith Wilson, Deputy Chief Auditor**

## **Division of Registration and Inspections**

**Helen A. Munter, Director**

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# ***PCAOB***

- Auditor independence and Audit Firm rotation
- Auditor Reporting Model
- Transparency of audits
- Auditing Standard No. 16,  
*Communications with Audit Committees*