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THE NEWSLETTER FROM BDO'S NATIONAL ASSURANCE PRACTICE

BDO KNOWS: SEC

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SEC YEAR IN REVIEW

SIGNIFICANT 2015 DEVELOPMENTS

Consistent with Chair White's focus over the past few years, the Commission's 2015 agenda continued to be dominated by rulemaking required by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and the Jumpstart Our Business Startups (JOBS) Act of 2012. The Commission made progress on the backlog of Dodd-Frank rulemaking related to executive compensation matters, including a final rule on pay ratio disclosures and proposals on pay vs. performance disclosures and compensation clawback policies. In December, the Commission re-proposed a rule to require resource extraction issuers to disclose payments made to the U.S. and foreign governments. The re-proposal followed a Court decision in July 2013 to vacate the rule requiring disclosure of the same information that the SEC adopted in 2012. The Commission also completed all of the major rulemaking required by the JOBS Act, including final rules related to crowdfunding and amendments to Regulation A. The Commission and its staff now need to focus on implementing the provisions of the Fixing America's Surface Transportation (FAST) Act, which was passed in December and included provisions that amend securities laws, some of which became effective immediately.

There were several notable changes in the Commission and the staff in 2015. Daniel Gallagher (Republican) left the Commission in October. Luis Aguilar (Democrat) also announced his intention to leave the Commission at the end of December or earlier if his replacement is confirmed. The President nominated two individuals, Hester Peirce

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(Republican) and Lisa Fairfax (Democrat), though they have yet to be confirmed by the Senate. At the staff level, Wes Bricker replaced Dan Murdock as a Deputy Chief Accountant in the Office of the Chief Accountant.

The SEC's Chief Accountant, James Schnurr, continued to lead the Commission's work on deciding whether, and if so, how and when, to incorporate International Financial Reporting Standards into financial reporting by domestic issuers. The idea currently being considered is to permit domestic issuers to voluntarily provide IFRS-based financial information as a supplement to their U.S. GAAP financial statements without requiring a reconciliation to U.S. GAAP (as is otherwise required when non-GAAP financial information is presented). In December, Chair White indicated that the Commissioners will be discussing this recommendation with the staff to determine the path forward.

Schnurr and his staff have also been focused on addressing implementation issues related to the new revenue accounting standard and other pending standards on leases, classification and measurement of financial instruments, and credit losses. The staff has expressed concern that many companies are not as far along as they should be in their implementation efforts and has been using speeches to encourage them to step up the pace of their activities.

The Commission and the staff remain focused on the Disclosure Effectiveness Project, a broad-based staff review of the SEC's disclosure rules designed to improve the disclosure regime for both companies and investors. In September, the Commission issued a Request for Comment about the financial disclosures of entities other than the registrant. Another disclosure topic that the Commission is revisiting is disclosures by audit committees about their activities. The rules covering these disclosures have not been updated since 1999, and the Commission is concerned that the rules may not have kept pace with the evolving role and responsibilities of audit committees. To solicit input, the Commission issued a concept release, *Possible Revisions to Audit Committee Disclosures*.

The staff issued guidance throughout the year to assist registrants and others with interpreting and complying with the SEC's rules and regulations. The staff updated its Compliance and Disclosure Interpretations (C&DIs) and the Financial Reporting Manual (FRM) and issued small business compliance guides covering the new rules adopted to implement the JOBS Act.

Looking forward to 2016, the remaining rulemaking required by the Dodd-Frank Act is expected to remain a high priority of the Commission, as well as the new rulemaking required by the FAST Act. The Commission also hopes to make a further statement about the use of IFRS by domestic issuers. The staff is expected to make progress on the Disclosure Effectiveness Project and address implementation issues and concerns related to the new revenue standard and other pending accounting standards.

This publication summarizes 2015 Commission and staff activities that affect financial reporting. We discuss rulemaking first, followed by staff guidance provided during 2015. While not the focus of this publication, we also discuss the PCAOB's 2015 standard-setting and related activities.

IMPLEMENTING LEGISLATION

THE DODD-FRANK ACT

Pay Ratio Disclosure

(Release No. 33-9877)

In August, the SEC adopted, by a 3-2 vote, a rule mandated by Section 953(b) of the Dodd-Frank Act. The rule amended Item 402 of Regulation S-K and requires issuers to disclose the following:

- The median annual total compensation of all employees except the chief executive officer;
- The annual total compensation of the CEO; and
- The ratio of the median annual total compensation of all employees to the annual total compensation of the CEO.

These disclosures are collectively referred to as the "pay ratio" disclosures and are intended to help inform shareholders when evaluating a CEO's compensation. The rule is generally consistent with the one the SEC proposed in 2013. The adopting release is available here on the SEC's website.

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The pay ratio disclosures are required in any annual report, proxy, or registration statement that requires disclosure of executive compensation pursuant to Item 402 of Regulation S-K. However, emerging growth companies, smaller reporting companies, foreign private issuers, Multijurisdictional Disclosure System filers, and registered investment companies are exempt from the requirements. In addition, companies filing initial registration statements (whether in an initial public offering or on Form 10) are not required to provide the pay ratio disclosures. Certain transition relief is available for newly public companies, companies with business combination activity, and those exiting smaller reporting company or emerging growth company status.

Companies are required to provide the pay ratio disclosures for their first fiscal year beginning on or after January 1, 2017. For example, a registrant with a fiscal year ending on December 31 would be first required to include the pay ratio information relating to compensation for fiscal year 2017 in its proxy or information statement for its 2018 annual meeting of shareholders and to include or incorporate by reference this information in its 2017 Form 10-K.

The rule requires a registrant to (1) determine the employee whose annual total compensation level is the median of all of its employees except its CEO, (2) compute the median employee's total compensation, and (3) compute a ratio in which the median employee's total compensation is equal to 1 and the CEO's total compensation is a calculated number. For example, if the amount of the median employee's total compensation is $45,790 and the CEO's total compensation is $12,260,000, then the pay ratio disclosed would be "1 to 268". The ratio could also be expressed narratively, such as "the CEO's annual total compensation is 268 times that of the median of the annual total compensation of all employees."

Subject to certain exceptions described below, the median employee is identified by an analysis of the annual compensation of all persons, including all U.S. and non-U.S. full-time, part-time, seasonal, and temporary workers, employed by the registrant and its consolidated subsidiaries as of any date within the last three months of its fiscal year.[1] The individual compensation amounts used to identify the median employee may be annualized for permanent employees who were employed for less than the full fiscal year. Such amounts for seasonal and temporary workers may not be annualized. Similarly, such amounts for part-time workers may not be adjusted to the full time equivalent amount. The rule permits registrants to identify the median employee in a variety of ways. For example, a registrant is permitted to analyze its entire employee population, use a statistical sampling methodology, or any other reasonable method. Moreover, the median employee can be determined using a consistently applied compensation measure (e.g., amounts derived from the registrant's payroll or tax records), rather than each employee's total compensation. Once the median employee is identified, that person's annual total compensation pursuant to Item 402(c)(2)(x)[2] must be calculated and disclosed. The rule permits companies to make estimates when calculating the elements of annual total compensation in accordance with Item 402. Disclosure of the methodology and material assumptions and estimates used to identify the median employee and/or determine the compensation amounts is required. Registrants are permitted to supplement the disclosure with additional narrative discussion or other ratios as long as the information is clearly identified and is not given greater prominence than the prescribed pay ratio disclosures.

The final rule contains changes from the proposal that are intended to provide companies with flexibility to meet the rule's requirements in a number of other ways, including the ability to:

- Identify the median employee only once every three years. However, if there has been any change in the employee population or employee compensation arrangements which may result in a significant change to the pay ratio, the median employee should be re-identified. If the median employee's compensation significantly changes during the three year period, the company may use another employee with substantially similar compensation as the median employee.
- Exclude non-U.S. employees from countries in which obtaining the required information to calculate the pay ratio would violate the particular jurisdiction's data privacy laws or regulations (i.e., the data privacy exception). This exception can only be applied if the Company obtains a legal opinion supporting the assertion that obtaining the necessary information violates the local laws.
- Exclude up to 5% of its total employees who are non-U.S. employees (i.e., the de minimis exception), which includes any non-U.S. employees excluded under the data privacy exception. This exception can only be applied on a jurisdiction by jurisdiction basis, so that if one employee in a jurisdiction is excluded all must be excluded.

1 Independent contractors and leased employees are excluded from this population.
2 Total compensation per Item 402(c)(2)(x) includes salary, bonus, the aggregate grant date fair value of options or stock awarded during the period, earnings for services performed under non-equity incentive plans and all earnings on any outstanding awards, certain amounts related to defined benefit and actuarial pension plans, and any other compensation not included in the aforementioned categories.

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- Apply an adjustment to account for differences between the cost-of-living in the CEO's jurisdiction and the cost-of-living in other jurisdictions when identifying the median employee. If applied, the same adjustment would be made to the median employee's annual total compensation used to calculate the pay ratio. However, disclosure of the compensation amount and pay ratio without the cost-of-living adjustment is still required.

Pay vs. Performance Disclosure

(Release No. 34-74835)

In April, the SEC proposed rules which would implement requirements mandated by Section 953(a) of the Dodd-Frank Act. The proposed rules would require registrants to disclose in a clear manner the relationship between executive compensation actually paid and the financial performance of the registrant. The proposed rules are intended to help shareholders to be better informed when they vote to elect directors and in connection with advisory votes on executive compensation.

Proposed Item 402(v) of Regulation S-K would require registrants to provide the table shown below comparing the (i) executive compensation actually paid to the named executive officers for whom disclosure is currently required in the Summary Compensation Table (SCT); (ii) Total Shareholder Return (TSR) for the registrant and; (iii) TSR for the selected peer group.

Year	SCT Total for Principal Executive Officer (PEO)	Compensation Actually Paid to PEO	Average SCT Total for non-PEO Named Executive Officers	Average Compensation Actually Paid to non-PEO Named Executive Officers	Total TSR	Peer Group TSR
(a)	(b)	(c)	(d)	(e)	(f)	(g)

Executive compensation actually paid will be different than the total compensation reported in the SCT. Executive compensation actually paid is total compensation as reported in the SCT for the year (i) less the change in the actuarial present value of pension benefits, (ii) less the grant-date value of any stock and option awards granted during the year that are subject to vesting, (iii) plus the actuarially determined service cost for services rendered during the applicable year, and (iv) plus the value at the vesting date of stock and option awards that vested during that year. The executive compensation would be presented separately for the PEO and as an average for the remaining named executive officers identified in the table.

TSR would use the definition included in Item 201(e) of Regulation S-K (i.e., dividends plus or minus change in share price) and TSR for the selected peer group would use the peer group identified by the company in its stock performance graph or in its compensation discussion and analysis.

Using the values presented in the table, proposed Item 402(v) would require the registrant to describe (1) the relationship between the executive compensation actually paid and registrant TSR, and (2) the relationship between registrant TSR and peer group TSR. Such disclosures would follow the table and could be presented as a narrative, graphically, or a combination of the two.

Other Highlights of the Proposed Rules

- The disclosure would be required in proxy or information statements in which executive compensation disclosure is required.
- The rules would apply to all reporting companies except for foreign private issuers, registered investment companies and emerging growth companies.
- The disclosure would be required for the last three fiscal years for smaller reporting companies and last five fiscal years for any other registrants. Smaller reporting companies would not be required to present a peer group TSR.

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- The disclosure would be tagged in an interactive data format using eXtensible Business Reporting Language, or XBRL. Tagging would be phased in for smaller reporting companies, so that they would not be required to comply with the tagging requirement until the third annual filing in which the pay-versus-performance disclosure is provided.

- The phase-in period would be as follows: Smaller reporting companies would initially provide the information for two years, adding an additional year in their subsequent annual proxy or information statement that requires this disclosure. Other registrants would be required to provide the information for three years in the first proxy or information statement in which they provide the disclosure, adding another year of disclosure in each of the two subsequent annual proxy statements that require this disclosure.

The proposing release is available here. Comments on the proposal were due in July.

Clawbacks of Executive Compensation

(Release No. 33-9861)

In July, the SEC proposed a rule which would require national securities exchanges to establish standards for listed companies that would require the clawback of erroneous executive compensation. The rule would implement provisions mandated by Section 954 of the Dodd-Frank Act. These standards would force listed companies to establish and enforce policies that require executives to pay back certain incentive-based compensation that was erroneously awarded. Proposed Rule 10D-1 would substantially increase the existing requirements covering recovery of executive compensation in Section 304 of the Sarbanes-Oxley Act, which requires the CEO and CFO to reimburse an issuer for certain compensation when an accounting restatement which resulted from misconduct occurred during the preceding twelve months.

The clawback provisions of Rule 10D-1 would require a listed company, upon restating its financial statements, to calculate the difference between the amount of incentive-based compensation awarded to an executive and the amount that would have been awarded had the financial statements properly reflected the restated amounts. This calculation would be performed for the three fiscal years prior to the date that a restatement was required. The excess amount that was erroneously awarded would be recovered from both current and former executives of the listed company. The population of "executives" from which recovery would be required is broader than under the Sarbanes-Oxley Act and includes any person who performs policy-making functions for the company. For example, roles such as the company's president, principal financial officer, principal accounting officer, and any vice-president in charge of a principal business unit, division or function would be included in the definition of an executive. The proposal takes a "no fault" approach. There is no consideration of whether there was any misconduct by an executive or whether an executive had responsibility for the erroneous financial statements.

Incentive-based compensation subject to recovery includes compensation that was determined based upon the attainment of financial reporting measures. Financial reporting measures are those based upon accounting principles used in preparing the financial statements, any measures derived from that financial information, stock price, and Total Shareholder Return (TSR). Other compensation, such as compensation based upon continued employment and compensation awarded at the discretion of the board of directors, would be excluded from this provision. A company would be required to make a reasonable estimate of the effect of the erroneous accounting on the stock price and TSR.

A company that does not adopt a policy for the recovery of erroneously awarded incentive-based compensation, enforce the policy, or comply with the disclosure provisions of the rule would be subject to delisting.

Other Highlights of the Proposed Rules

- Proposed Rule 10D-1 would apply to all listed companies, except for certain registered investment companies that do not provide incentive-based compensation to their employees. Smaller reporting companies, emerging growth companies, and foreign private issuers (FPIs) would all be subject to the new listing standards.

- A company would have the discretion to not enforce the recovery of incentive-based compensation only if the costs related to the recovery are expected to exceed the amount to be recovered or, for FPIs, if the recovery violates home country laws.

- Executives could not be indemnified.

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- Other proposed rule changes would require companies to disclose their recovery policies and how they have applied them. The recovery policy would be filed as an exhibit to the annual report. Additional disclosures would be required in annual reports and proxy statements when a restatement occurred or there is a continuing outstanding balance of excess incentive-based compensation that has not been recovered. These additional disclosures would include:

  - Date of restatement
  - If restatement is subject to recovery
  - Amount of the excess balance to be recovered
  - Amount remaining outstanding
  - How estimates of stock price and TSR were calculated
  - Name of individual for which the Company chose not to pursue collection
  - Name of individual that hasn't paid within 180 days

- The disclosure would be block tagged in an interactive data format using eXtensible Business Reporting Language, or XBRL.

- Following the publication of the adopted version of Rule 10D-1, the exchanges would have 90 days to file their proposed listing rules and those listing rules would be required to become effective within one year of the date Rule 10D-1 is published. The recovery policy for each listed company must be adopted within 60 days after the exchange's rule becomes effective. All excess incentive-based compensation received by current and former executives on or after the effective date of Rule 10D-1 would be subject to recovery.

The proposing release is available here. Comments on the proposed rules were due in September.

BDO OBSERVATIONS:

Many issuers' reaction to this proposal has been fairly negative particularly from the perspective of some companies who view the proposal as too broad in its reach – i.e., the expansive list of policy-making employees that the rule would apply to and the no-fault approach taken in the release. Some have questioned whether the proposal would have some unintended consequences, such as the creation of a market for "clawback insurance" to insure executives against the future loss of compensation through no fault of their own. Some wonder whether the proposal would discourage companies from tying executive compensation to company performance measures (which seems counter-productive). Others have expressed concerns about how to reasonably determine what a company's stock price or TSR would have been if the erroneous accounting had not been applied in prior periods. How the SEC will respond to these concerns remains to be seen.

Disclosure of Payments made by Resource Extraction Issuers

(Release No. 34-76620)

In December, the SEC re-proposed Exchange Act Rule 13q-1, which was mandated by Section 1504 of the Dodd-Frank Act. Congress enacted Section 1504 to combat global corruption by promoting international transparency of payments made to governments for the commercial development of oil, natural gas, and minerals. Rule 13q-1 would require resource extraction issuers to disclose information about certain payments made to the United States and foreign governments. The proposing release can be accessed here. Comments on the proposed rule are due by January 25, 2016.

The Commission initially adopted Rule 13q-1 to satisfy the Act's statutory mandate in August 2012. However, following a lawsuit to overturn the rule filed by the American Petroleum Institute, the U.S. Chamber of Commerce and two other business groups, a federal court vacated the rule in July 2013. The court ruled that the SEC misread Section 1504 of the Act to require public disclosure of such information. The court also noted that the SEC's decision to deny any exemptions from the rule was "arbitrary and capricious." In response, the SEC has rewritten and re-proposed the rule. The Commission has also filed with a court a rulemaking schedule indicating that it will vote on a final rule in June 2016.

The proposal is substantially consistent with the rule adopted in 2012. The most significant changes are:

- The term "project" was defined.

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- The Commission will consider using its authority to grant requests for exemptive relief.

- As an alternative to the required report, issuers would be able to use a report prepared for foreign regulatory purposes if the SEC deems the requirements of the foreign regime to be substantially similar to the Commission's requirements.

The proposed rule would apply to "resource extraction issuers," defined as domestic and foreign issuers who are engaged in the commercial development of oil, natural gas, or minerals and are required to file an annual report under the Exchange Act. The activities that constitute "commercial development of oil, natural gas, or minerals" would include exploration, extraction, processing, export, or the acquisition of a license for any such activity.

Issuers would be required to disclose any payment (or series of related payments) to the U.S. government or foreign governments that is not de minimis (which the rule defines as equaling or exceeding $100,000 during a fiscal year) and has been made to further the commercial development of oil, natural gas, or minerals.

The disclosures would include, among other things, the type and total amount of payments made for each project and to each government.[3] As proposed, a project is contract-based and would be defined as the "operational activities that are governed by a single contract, license, lease, concession, or similar legal agreement, which form the basis for payment liabilities with a government." The proposal contains a non-exclusive list of factors to consider when determining whether two or more agreements may be treated as a single project for purposes of the disclosure.

Since Rule 13q-1 was first adopted in 2012, several international bodies and countries have adopted similar disclosure requirements. The European Union has adopted and Canada has proposed rules requiring similar disclosures. In light of these developments, the Commission proposed allowing issuers to use a report prepared for foreign regulatory purposes as discussed above.

The proposed location and timing of the disclosures are similar to the initial rule adopted in 2012. The disclosures would be filed annually in an XBRL-formatted exhibit to Form SD, which was created for the purpose of reporting the information required by this rule and the rule requiring disclosure of the use of conflict minerals. The report would be due 150 days after the end of an issuer's fiscal year. The proposed disclosures may be reported on a cash basis and would not need to be audited[4] or be subject to officer certifications.

THE JOBS ACT

Regulation A+

(Release No. 33-9741)

In March, the Commission unanimously approved amendments to Regulation A. The amendments, known as "Regulation A+," were required by Section 401 of the JOBS Act. They are intended to increase access to capital for smaller companies by modernizing Regulation A and expanding it to provide a streamlined process by which a private company can offer and sell up to $50 million of securities in a twelve-month period. The adopting release is available here. The amendments took effect on June 19.

Regulation A allows private companies to make small public offerings without having to register them with the SEC. Instead, the offering document must be reviewed and "qualified" by the SEC staff. Regulation A offerings have historically been subject to state-level registration and qualification requirements as well. Previously, Regulation A permitted offerings of up to $5 million of securities in a twelve-month period. Historically, very few offerings were made pursuant to Regulation A. The U.S. Government Accountability Office performed a study which identified the costs and complexity of state law compliance as one of the reasons for the lack of offerings using this exemption.

The amendments are intended to enhance the usefulness of Regulation A by increasing the amount of securities that can be offered in a twelve-month period to $50 million and streamlining the offering process by preempting state-level registration and qualification requirements if certain requirements are met.

3 The disclosure must include payments made by the issuer's subsidiaries or other entities it controls, by reference to the financial consolidation principles applied in the issuer's audited financial statements (e.g., a consolidated variable interest entity). Consequently, payments made by an issuer's equity method investee would generally not need to be reported.

4 Moreover, since Form SD would not include audited financial statements, auditors would not need to read the disclosures and consider whether they are materially inconsistent with the audited financial statements.

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Regulation A is available to U.S. and Canadian issuers that are not Exchange Act registrants. There are several other eligibility restrictions and rules governing the offering process and the amounts of securities that can be sold to various categories of investors in various scenarios.

The amendments created two tiers of offerings:

- Tier 1 – A modernized version of the historical Regulation A, Tier 1 permits offerings of up to $20 million in a twelve-month period. State securities regulators will continue their current role in Tier 1 offerings.

- Tier 2 – This new tier permits offerings of up to $50 million in a twelve-month period. State securities law requirements are preempted by Federal securities laws for these offerings.

Because Tier 2 offerings may generally involve larger dollar amounts and less state regulation, they are subject to more stringent requirements than Tier 1 offerings. Generally, the offering process and the ongoing reporting required after a Tier 2 offering are essentially scaled down versions of the offering and ongoing reporting processes used during and after registered offerings. Following is a general overview of Regulation A's revised financial reporting requirements.

Offering Circulars

Offering circulars must comply with the information requirements of revised Form 1-A, which requires the following:

- Offering circulars must contain two years of annual financial statements for the issuer and its predecessors. The financial statements must comply with U.S. GAAP or, for Canadian companies, IFRS as issued by the IASB; however, they need not comply with the incremental requirements of Regulation S-X. Financial statements must be updated every six months after they become nine months old. For example, an issuer with a December 31, 2014 year-end would need to provide comparative half year financial statements for the six months ended June 30, 2015 if its offering circular is filed or qualified after September 30, 2015. Similarly, that issuer would need to provide 2015 annual financial statements if its offering circular is filed or qualified after March 31, 2016.

- Offering circulars must contain financial statements of certain other entities (businesses and real estate operations acquired or to be acquired, guarantors and collateral entities (but not equity method investees)) and pro forma information.

- For new accounting standards that apply to both public and non-public business entities, an issuer may elect to delay complying with the standards until the dates non-public business entities must apply them, similar to the approach emerging growth companies may use. However, issuers in Regulation A offerings are considered public business entities, so they are not eligible to use alternative accounting standards available only to non-public business entities.

- Offering circulars must be filed via the SEC's EDGAR system. Exhibits providing data in XBRL format are not required.

- Issuers may submit offering circulars to the SEC staff for review on a confidential basis before they are filed publicly, similar to the process used in registered offerings by emerging growth companies.

The audit requirements for the historical financial statements discussed above vary depending on whether the offering is a Tier 1 or a Tier 2 offering.

- In Tier 1 offerings, the financial statements must be audited only if an audit has been obtained for another purpose. Such audits may be performed (a) in accordance with U.S. GAAS or PCAOB standards, (b) by auditors who are not registered with the PCAOB, and (c) by auditors who are independent pursuant to either AICPA or SEC independence standards.

- In Tier 2 offerings, the financial statements must be audited. Similar to the audit requirements for Tier 1 offerings, such audits may be performed in accordance with U.S. GAAS or PCAOB standards and by auditors who are not registered with the PCAOB. In contrast, the auditors' report must comply with Article 2 of Regulation S-X and the auditor must meet the SEC's independence standards.

Ongoing Reporting

The only subsequent reporting required of an issuer that has conducted a Tier 1 offering is to file a new Form 1-Z. This report is due 30 days after termination or completion of the offering and provides information about the results of the offering (e.g., number of securities sold, proceeds, etc.).

An issuer that has conducted a Tier 2 offering must file the following reports on an ongoing basis:

- Annual reports on new Form 1-K – Form 1-K is due no later than 120 days after year-end. The report must contain two years of issuer audited financial statements and audited financial statements of guarantors and collateral entities. The audit requirements are the same as discussed above for a Tier 2 offering.

- Semiannual reports on new Form 1-SA – Form 1-SA is due no later than 90 days after the end of the first half of an issuer's fiscal year. The report must contain financial statements similar to those in a Form 10-Q, except only year to date financial statements are required (i.e., no quarterly financial statements are required) and the financial statements are not required to be reviewed by the issuer's auditor.

- Current reports on new Form 1-U – Similar to Form 8-K, Form 1-U requires reporting of significant current events and is due four business days after a reportable event occurs. The types of events to be reported are similar to Form 8-K, but the threshold for reporting acquisitions and divestitures is much higher and no historical or pro forma financial statements are required.

- Similar to the requirements for offering circulars, ongoing reports must be filed via the SEC's EDGAR system, exhibits providing data in XBRL format are not required, and the financial statements may not be prepared using alternative accounting standards available only to non-public business entities.

Issuers in Tier 2 offerings also use Form 1-Z, but generally for a different purpose than that for which Tier 1 issuers use it. An issuer in a Tier 2 offering uses this form to notify the SEC when its reporting obligations have terminated and it will stop ongoing reporting.

In June, the SEC staff issued a small entity compliance guide to assist companies with the application of the rule; it is available here on the SEC's website.

BDO OBSERVATIONS:

As mentioned above, very few offerings were conducted under Regulation A historically. We understand that while acceptance and use of Regulation A+ has been limited thus far, it is currently being used much more than Regulation A was used in the past.

THE FAST ACT

The President signed the Fixing America's Surface Transportation (FAST) Act into law in December.[5] While the Act is focused on providing transportation funding, certain provisions of the Act amend the securities laws. Some of the amendments are self-executing, while others require SEC rulemaking.

The amendments included in Title LXXI of the Act are intended to improve access to capital for emerging growth companies. Unless otherwise noted below, the provisions related to Title LXXI are effective immediately. These amendments:

- Reduce the number of days an EGC's confidential submissions must be made public before its IPO roadshow to 15 days. EGCs are permitted to submit an IPO registration statement confidentially for review by the SEC staff. A confidentially submitted initial registration statement and subsequent amendments were previously required to be made public 21 days prior to the IPO roadshow.

- Permit an issuer that qualifies as an EGC at the time its initial registration statement is filed or submitted to maintain its EGC status even if it is otherwise lost until the earlier of:

5 The text of the Act is available here.

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- The issuer's completed initial public offering, or
- One year after the date on which the issuer lost its EGC status.

For example, if an issuer submitted its initial registration statement as an EGC but crossed the $1 billion revenue threshold before going effective, it would be permitted to maintain its EGC status until the earlier of the dates mentioned above.

- Permit an EGC to omit historical periods from its financial statements if it reasonably expects that such periods will not be included in its effective registration statement. For example, if a calendar year end EGC submits its initial registration statement in December 2015 for confidential review by the SEC staff, the SEC's rules required the EGC to present its financial statements for the years 2013 and 2014 and the nine months ended September 30, 2014 and 2015. The FAST Act allows an EGC to omit the 2013 financial statements if it reasonably expects that the 2013 period will not be included in the effective registration statement (i.e., if the registrant in this example expects to present full year 2014 and 2015 financial statements in the registration statement when it becomes effective in 2016).

The SEC staff subsequently issued two Compliance and Disclosure Interpretations related to the provision above (available here on the SEC's website). The guidance indicates an EGC:

- May omit financial statements of other entities from its filings or submissions (e.g., Rule 3-05 target financial statements) if it reasonably expects such financial statements will not be required at the time of the offering.

- May not omit interim financial statements from its filings or submissions if the interim period or longer period (interim or annual) has been or will be included in the required financial statements at the time of the offering. For example, a calendar year end EGC that expects to commence its offering in April 2016 may not omit its 2014 and 2015 nine-month interims from its filings or submissions as they relate to the annual periods that will be required at the time of the offering.

Other self-executing changes add a new exemption for secondary sales of securities that are purchased by accredited investors and revise Section 12(g) of the Exchange Act so that savings and loan holding companies are treated the same as banks and bank holding companies for purposes of registration, termination of registration or suspension of their Exchange Act reporting obligations.[6] The SEC staff subsequently issued four Compliance and Disclosure Interpretations related to this provision (available here on the SEC's website).

Other significant changes to securities laws included in the FAST Act which require SEC rulemaking or additional analysis will:

- Permit smaller reporting companies to forward incorporate information by reference into Form S-1. Consequently, these companies will be able to update an effective registration statement without filing an amendment. This will facilitate offerings such as secondary offerings by selling shareholders. However, it will not permit delayed shelf offerings by such issuers, because Securities Act Rule 415(a)(1)(x) requires such offerings to be registered on Form S-3 or F-3. The amendments to Form S-1 are required by January 18, 2016.

- Require the SEC to conduct a study on the disclosure requirements of Regulation S-K with a goal to modernize and simplify its requirements. The study and the Commission's corresponding recommendations are due to Congress by November 28, 2016.

- Require the SEC to revise Regulation S-K to determine how to scale or eliminate the requirements for filers other than large accelerated filers and eliminate duplicative, outdated, or unnecessary disclosures for all filers. These changes are required by June 1, 2016 unless further consideration is needed under the study mentioned above.

- Permit issuers to include a summary page on Form 10-K that cross-references to other sections in Form 10-K. Currently, a registrant is not prohibited from including a summary, but the FAST Act adds a provision which specifically allows it and requires cross-referencing. Rulemaking is required by June 1, 2016.

Further information on the FAST Act can be found here on the SEC's website.

6 The JOBS Act raised the number of shareholders of record a company may have before SEC registration is required from 500 to 2,000 as long as there are less than 500 shareholders who are not accredited investors. Nonpublic banks and bank holding companies are not subject to the 500 unaccredited investor threshold. The JOBS Act also raised the number of shareholders of record a bank or bank holding company must be below in order to terminate its SEC registration from 300 to 1,200.

OTHER COMMISSION ACTIVITIES

REQUEST FOR COMMENT — FINANCIAL DISCLOSURES ABOUT ENTITIES OTHER THAN THE REGISTRANT

In September, the SEC published a request for comment on the effectiveness of certain financial disclosure requirements of Regulation S-X. The request is part of the Disclosure Effectiveness Project, a broad-based staff review of the SEC's disclosure rules designed to improve the disclosure regime for both companies and investors.

The request for comment focuses on the disclosure requirements for entities other than a registrant, including those of acquired businesses (under Rule 3-05), subsidiaries not consolidated and 50 percent or less owned persons (under Rules 3-09 and 4-08(g)), guarantors and issuers of guaranteed securities (under Rule 3-10), and affiliates whose securities collateralize registered securities (under Rule 3-16). The request contains questions directed to investors and registrants about:

- How the required financial information is utilized
- What changes could be made to improve its usefulness
- What challenges registrants face in preparing such information
- Whether the bright-line tests required by some of the rules should be revised
- Whether judgment should enter into the determination to provide some of the financial information, etc.

The request for comment can be found here on the SEC's website. Comments on the project, which were due on November 30, and additional information can be found here on the SEC's website.

BDO OBSERVATIONS:

We support the Commission's initiative to review and consider ways to improve the effectiveness of the financial disclosure regime under Regulations S-X and S-K. While we ultimately defer to investors about how certain disclosures are used to make investing and voting decisions, we question the utility of some of the financial information required by rules for entities other than the registrant. Our comment letter on the request (available here) provides suggestions that we believe, if implemented, could improve or simplify the disclosure requirements without sacrificing their objectives.

CONCEPT RELEASE ON POSSIBLE REVISIONS TO AUDIT COMMITTEE DISCLOSURES

In July, the SEC issued a concept release seeking public comment regarding audit committee reporting requirements. The concept release was issued in response to views that the SEC's existing disclosure rules perhaps have not kept pace with the evolving role and responsibilities of audit committees and may not result in disclosures about audit committees and their activities that are sufficient to help investors understand and evaluate audit committee performance, which may in turn inform investors' investment or voting decisions.

Some of the more significant potential changes to reporting requirements being considered include how an audit committee discharges its responsibilities with respect to its oversight of the auditor, the process for selecting the auditor, and consideration of the qualifications of the audit firm and certain members of the engagement team when selecting the audit firm.

Comments on the release were due in September.

Read more

BDO OBSERVATIONS:

Our comment letter supports the SEC's efforts to explore ways to enhance an audit committee's disclosure about how an audit committee discharges its responsibilities. We further support the SEC's efforts to update its existing disclosure requirements to include updated references to required communications between auditors and audit committees contained in PCAOB Auditing Standards. We expressed concern that the SEC's focus on the oversight of the external auditor represents only part of the audit committee's responsibilities with respect to its oversight of a company's accounting and financial reporting process. Similar to our commentary regarding the PCAOB's concept release on Audit Quality Indicators, we expressed overall support for a flexible, voluntary approach that would allow audit committees to design disclosures in accordance with the needs of their specific investor communities. The voluntary disclosures could then correspond with the nature and extent of the organization's unique challenges and opportunities and could best reflect the scope of the audit committees' actual specific processes. This flexible and voluntary approach would also avoid the risk of "chilled communications" between the audit committee and the auditor as well as potential "boilerplate" or "check the box" disclosures that may result from mandating disclosures. We further highlighted publicized findings that indicate many audit committees are already voluntarily providing more enhanced disclosures about the execution of their duties. Additionally, where there are concurrent rule-making and standard-setting initiatives being undertaken by the SEC and PCAOB that potentially complement each other (e.g., auditor reporting and transparency, disclosure of critical audit matters, audit quality indicators, etc.), we strongly encouraged the SEC to continue to work collaboratively with the PCAOB in issuing guidance related to public companies audits. Our comment letter is available here.

STAFF GUIDANCE

Notable guidance the SEC staff provided during 2015 is discussed below. Some of the guidance was provided during meetings held with the Center for Audit Quality's (CAQ's) SEC Regulations Committee. Minutes of those meetings can be found here on the CAQ's website.

PUSHDOWN ACCOUNTING AND RULE 3-10

Last year, in connection with the FASB's issuance of ASU 2014-17, *Pushdown Accounting*, the SEC staff issued Staff Accounting Bulletin No. 115 to rescind its legacy pushdown guidance for SEC registrants in Topic 5.J, *New Basis of Accounting Required in Certain Circumstances*. Further information on the guidance in ASU 2014-17 can be found here.

Registrants should follow GAAP when preparing condensed consolidating financial information to comply with Rule 3-10. Therefore, we understand that if pushdown accounting is applied in a subsidiary's financial statements, it should also be applied when compiling the information presented under Rule 3-10(i).

REPORTING IMPLICATIONS OF THE NEW CONSOLIDATION STANDARD

In February, the FASB issued ASU 2015-02, *Amendments to the Consolidation Analysis,* which changes the consolidation analysis for all reporting entities. The changes primarily affect the consolidation of limited partnerships and their equivalents (e.g., limited liability corporations), as well as structured vehicles such as issuers of collateralized debt obligations. The amendments are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015, although early adoption is permitted. The amendments may be applied using a modified retrospective approach or a full retrospective approach.[7] At the March meeting of the CAQ SEC Regulations Committee, the SEC staff clarified several reporting questions related to the adoption of the new standard:

- Consolidation or deconsolidation as a result of adopting ASU 2015-02 is not an event that needs to be reported under Item 2.01 of Form 8-K. Conversely, consolidation or deconsolidation as a result of reconsideration events subsequent to adoption would need to be considered for reporting under Item 2.01.

7 Further information regarding ASU 2015-02 can be found here.

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- Registrants who adopt the standard retrospectively should consider the need to revise the historical financial statements when filing a new or amended registration statement or proxy statement. However, registrants need not apply the standard to periods not covered by the audited financial statements (e.g., in the earliest two years presented in the selected financial data table).

- In the initial year of consolidation, a registrant may analogize to the SEC staff guidance in FAQ #3[8] when considering whether to scope a newly consolidated entity into management's assessment of internal control over financial reporting. FAQ #3 permits a registrant to exclude a newly acquired business from its internal control assessment if the time period between the acquisition date and the assessment date is not considered adequate for management to complete its testing.

PRO FORMA RESERVES AND SMOG DATA

Accounting Standards Codification section 932-235 requires oil and gas companies to disclose supplemental information about reserve quantities and a standardized measure of discounted future net cash flows (SMOG) in the historical financial statements. Such disclosures should also be provided in the historical financial statements of acquired oil and gas businesses (based on the guidance in FRM paragraph 2065.2). Item 914 of Regulation S-K requires additional pro forma information including a pro forma statement of cash flows, pro forma book value per share, and pro forma oil and gas reserve data for roll-up transactions as defined in Item 901 of Regulation S-K.

At the June meeting of the CAQ SEC Regulations Committee, the SEC staff indicated that it also expects to see pro forma reserves and SMOG disclosures in the pro forma financial statements associated with significant acquisitions of oil and gas businesses. In practice, similar disclosures are not typically provided in pro forma financial statements related to dispositions of oil and gas businesses.

FINANCIAL REPORTING MANUAL

The staff of the SEC's Division of Corporation Finance published two updates to the *Financial Reporting Manual* (FRM) in 2015.[9] As updates are published, the staff includes a summary immediately following the FRM cover that describes the nature of the changes and lists the paragraphs that were updated. The staff also annotates the FRM to communicate the date a paragraph was most recently updated.

The January update made minor, non-substantive wording changes and other revisions to conform to the issuance of ASU 2014-17, *Pushdown Accounting*, and corresponding rescission of SAB Topic 5.J, *New Basis of Accounting Required in Certain Circumstances,* discussed above.

The August update amended paragraphs 1320.3 and 1320.4 and provided guidance for registrants with delinquent filings who seek to become current by presenting all information that would have been included in the delinquent filings in a comprehensive annual report on Form 10-K. The guidance indicates that the staff will generally not issue comments asking a delinquent registrant to file separately all of its delinquent filings if the registrant takes this approach.

The FRM is available here on the SEC's website.

COMPLIANCE AND DISCLOSURE INTERPRETATIONS

The SEC staff updated its C&DIs several times during the year. The updates provided guidance on the FAST Act, Regulation A+ and various other legal topics including those related to Securities Act rules and forms, among others.

The C&DIs are available here on the SEC's website.

8 Frequently Asked Question Number 3 on management's report on internal control over financial reporting and certification of disclosure in Exchange Act periodic reports

9 The FRM is an internal SEC staff reference document that provides general guidance covering several SEC reporting topics. While the FRM is not authoritative, it is often a helpful source of guidance for evaluating SEC reporting issues. The FRM, along with other helpful guidance, can be accessed from the Division of Corporation Finance home page, which is located here.

STAFF ACTIVITIES

During 2015, the SEC staff continued to focus on issues related to implementing the new revenue accounting standard and on the Disclosure Effectiveness Project. Other staff activities and focus areas which may not have resulted in formal staff guidance can be found in our report on the AICPA Conference on SEC and PCAOB Developments held in December.

IMPLEMENTING THE NEW REVENUE STANDARD

ASU 2014-09, *Revenue Recognition,* is now scheduled to take effect in 2018 for public entities and establishes a comprehensive revenue recognition standard for virtually all industries. The SEC staff continues to focus on issues related to implementing the new standard. In October, at the CAQ SEC Regulations Committee meeting, the staff discussed the following implementation issues related to the interaction between the standard and certain SEC rules. We understand that:

1. Consistent with current guidance,[10] registrants that adopt the new standard on a full retrospective basis should remeasure significance of equity method investees for all periods.

2. The staff will not object if companies do not recast the earliest two years presented in the ratio of earnings to fixed charges table if they adopt the standard using a full retrospective approach. That is, a company would be required to reflect the accounting change in its ratio of earnings to fixed charges table only for the three years for which it presents full financial statements elsewhere in the filing.

3. Based on the requirements of Item 11(b) of Form S-3 and consistent with existing staff guidance[11] related to retrospective adoption of a new accounting principle, companies filing a new or amended registration statement will need to revise their financial statements for periods that precede the adoption date when financial statements for periods that include the adoption date are presented.

BDO OBSERVATIONS:

The SEC staff continues to stress the importance of timely and thoughtful implementation efforts prior to the adoption date. Wes Bricker, Deputy Chief Accountant, has conveyed several key implementation messages in recent speeches (available here and as discussed in our report on the AICPA conference) which focus on upgrading registrants' resources and internal controls over financial reporting. He has also cautioned against making conclusions that are designed to preserve the current accounting. SEC staff activities related to implementation and reporting issues associated with the new revenue standard are expected to continue as the adoption date approaches.

DISCLOSURE EFFECTIVENESS PROJECT

In addition to the *Request for Comment on Financial Disclosures about Entities Other than the Registrant* discussed above, the staff continues to study other areas for improving disclosure effectiveness, including working with the FASB to eliminate duplicate disclosure requirements and evaluating the disclosure requirements of Regulation S-K. The staff also continues to promote voluntary efforts by companies to improve the effectiveness of their disclosure by removing unnecessary duplication and disclosure of immaterial or outdated information. Further information regarding remarks of the SEC staff about disclosure effectiveness can be found in our report on the AICPA conference.

10 FRM Paragraph 2410.8
11 FRM Section 13100

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PCAOB DEVELOPMENTS

FINAL AUDITING STANDARDS AND AMENDMENTS

REORGANIZATION OF PCAOB AUDITING STANDARDS AND RELATED AMENDMENTS TO PCAOB STANDARDS AND RULES

In September, the SEC approved the PCAOB's proposed reorganization of PCAOB auditing standards and related changes to PCAOB rules and attestation, quality control, and ethics and independence standards. The reorganization, which was adopted by the PCAOB in March, uses a single, integrated numbering system. Under the reorganization, the individual standards are grouped into the following topical categories:

- *General Auditing Standards (section number 1000 - 1300)* —Standards on broad auditing principles, concepts, activities, and communications;
- *Audit Procedures (section number 2100 – 2900)* —Standards for planning and performing audit procedures and for obtaining audit evidence;
- *Auditor Reporting (section number 3100 – 3300)* —Standards for auditors' reports;
- *Matters Relating to Filings Under Federal Securities Laws (section number 4101 – 4105)* —Standards on certain auditor responsibilities relating to SEC filings for securities offerings and reviews of interim financial information; and
- *Other Matters Associated with Audits (section number 6101 – 6115)* —Standards for other work performed in conjunction with an audit of an issuer or of a broker or dealer.

The related amendments are technical changes that include rescinding certain interim auditing standards that the Board believes are no longer necessary and eliminating certain inoperative language or references. The amendments do not impose new requirements on auditors or change the substance of the requirements for performing and reporting on audits under PCAOB standards.

The reorganization and related amendments are effective as of December 31, 2016; however, auditors and others may use and reference the reorganized standards before the effective date. The reorganized standards are available here on the PCAOB's website.

DISCLOSURE OF ENGAGEMENT PARTNER AND CERTAIN OTHER AUDIT PARTICIPANTS

In December, the PCAOB adopted new rules (Rules 3210 and 3211) requiring audit firms to disclose the names of each audit engagement partner as well as the names of other audit firms that participated in each audit. Auditors will be required to file a new PCAOB Form AP, *Auditor Reporting of Certain Audit Participants*, for each issuer audit, disclosing:

- The name of the engagement partner;
- The names, location, and extent of participation of each other accounting firm participating in the audit whose work constituted 5 percent of the total audit hours; and
- The number and aggregate extent of participation of all other accounting firms that took part in the audit whose individual participation was less than 5 percent of the total audit hours.

The data reported on Form AP will be accessible through a searchable database on the PCAOB's website. The standard filing deadline for Form AP will be 35 days after the date the auditor's report is first included in a document filed with the SEC. In the case of initial public offerings, the Form AP filing deadline will be 10 days after the auditor's report is first included in a document filed with the SEC.

The disclosure requirement for the engagement partner will be effective for auditor's reports issued on or after January 31, 2017, or three months after SEC approval of the final rules, whichever is later. For disclosure of other audit firms participating in the audit, the requirement will be effective for reports issued on or after June 30, 2017.

PCAOB staff plans to publish guidance in 2016 relating to compliance with the reporting requirements of Form AP.

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OTHER STANDARD-SETTING ACTIVITIES

STAFF CONSULTATION PAPER

In May, the PCAOB issued a Staff Consultation Paper on standard-setting activities related to the auditor's use of the work of specialists, specifically the objectivity and oversight of specialists and the use of their work in audits. The PCAOB has observed that the use and importance of specialists has increased in recent years, in part due to the increasing complexity of business transactions and the resulting complexity of information needed to account for those transactions. The consultation paper raises questions about whether PCAOB standards adequately address the auditor's use of the work of specialists, and whether more rigorous standards and specific procedures are needed to help auditors respond to the risks of material misstatement in financial statements. The staff is seeking input on possible alternatives to address the issues discussed in the paper. Furthermore, the paper requests commenters to provide relevant economic data about potential economic impacts of standard-setting in this area.

The consultation paper is available here on the PCAOB's website. The comment period closed in July. In consideration of comments received that suggested that the Board coordinate the timing of this project with its project on auditing accounting estimates, including fair value measurements and related disclosures, the PCAOB staff plans to recommend that the Board closely coordinate the development and timing of any potential rulemaking for these two projects. The staff anticipates recommending that the Board propose for public comment revisions to its current standards on the auditor's use of the work of specialists by mid-2016.

BDO OBSERVATIONS:

Our comment letter supported the Board's consideration of amendments to PCAOB standards to clarify the way in which auditors use the work of specialists and provided specific recommendations for the Board's deliberation. Our comment letter is available here.

CONCEPT RELEASE ON AUDIT QUALITY INDICATORS

In June, the PCAOB issued a concept release seeking comment on the content and possible uses of audit quality indicators ("AQIs"). The concept release seeks comment on 28 potential AQIs at both the firm and engagement level that are intended to provide additional information about whether audit work being performed is being conducted by the appropriate individuals with the requisite experience, skills, resources, and tools. The potential AQIs cover the following:

- Audit Professionals — measures dealing with the availability, competence, and focus of those performing the audit
- Audit Process — measures concerning an audit firm's tone at the top and leadership, incentives, independence, investment in infrastructure needed to support quality auditing, and monitoring and remediation activities
- Audit Results — measures relating to financial statements (such as the number and impact of restatements, and measures of financial reporting quality), internal control over financial reporting, going concern reporting, communications between auditors and audit committees, and enforcement and litigation

The concept release also asks for views on how AQIs may best be used to promote audit quality. The concept release considers how AQI data might be obtained and distributed, whether use of AQIs should be optional or required, the scope of audits and audit firms that may be subject to AQI reporting, and how AQI reporting might be implemented over time.

The concept release is available here on the PCAOB's website. The comment period closed in September but was reopened through the end of November. It is the intention of the PCAOB, based on public comment, to reduce the number of AQIs to a more manageable and effective number for consideration in a future proposal.

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BDO OBSERVATIONS:

Our comment letter expressed support for the PCAOB's exploration of the use of AQIs in voluntary discussions with those concerned with the financial reporting and auditing processes, particularly the audit committee. We indicated support for a voluntary, principles-based approach to primarily engagement level AQIs that audit committees find most meaningful based on the facts and circumstances relative to the companies they serve. We strongly encouraged the PCAOB staff to conduct additional research regarding the relevance and usefulness of the proposed quantitative AQIs. In addition, we encouraged the PCAOB to further consider additional qualitative context that users of quantitative AQIs require in order to understand them. Our comment letter is available here.

GUIDANCE

AUDIT COMMITTEE DIALOGUE

In May, the PCAOB issued the first in a series of communications to audit committees intended to provide insights from inspections of public company audit engagements that may be helpful to audit committee members in overseeing their audit engagements. That communication, *The Audit Committee Dialogue*, highlights key areas of recurring issues in PCAOB inspections of large audit firms as well as certain emerging risks. The Dialogue also provides specific questions that committee members may ask their auditors on each topic. The Dialogue is available here on the PCAOB's website.

PCAOB DIALOGUES

In 2015, the PCAOB launched a podcast, PCAOB Dialogues, which features PCAOB Board members and staff speaking with audit committee members, investors, and others about auditing, investor protection, and capital markets issues. The first episode's topic was audit quality indicators. The podcast is available here.

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