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January 2022

Annual SEC and PCAOB update for public companies

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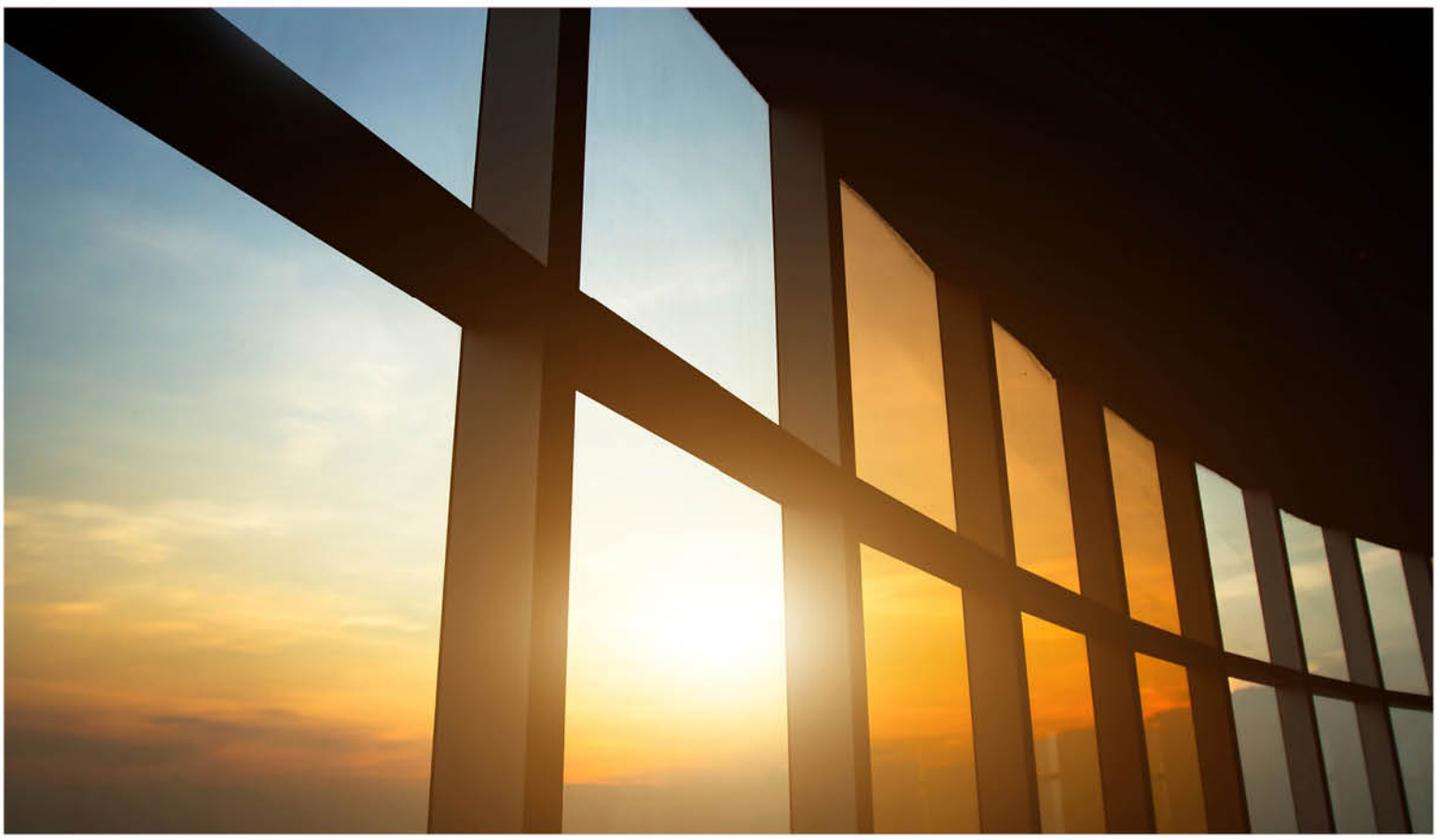

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From the authors

The end of the year brings conference season, and like the holiday season, conference season brings fun, festivities, and new insights about our collective financial reporting family. Early December 2021 was filled with updates from regulators, standard-setters, preparers, users, and other stakeholders at the annual AICPA & CIMA National Conference on SEC and PCAOB Developments, and we summarize key themes and messages.

SEC and PCAOB work during the entirety of 2021 reflects a quickly changing and dynamic financial reporting environment with challenges for all stakeholders, which likely will continue. As 2022 begins, we wish you, your family, and your friends a safe and happy new year.

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From the Securities and Exchange Commission (SEC)

Strategic plan

The SEC's current strategic plan features three goals:

- "Focus on the long-term interests of our Main Street investors. … Initiatives under this goal will include modernizing disclosure and expanding investor choice."
- "Recognize significant developments and trends in our evolving capital markets and adjust our efforts to ensure we are effectively allocating our resources … by analyzing market developments, evaluating existing rules and procedures, understanding the continually changing cyber-landscape and ensuring the appropriate resources are dedicated to each area."
- "Elevate the SEC's performance by enhancing our analytical capabilities and human capital development. The SEC will invest in data and technology."

Messages from SEC leadership

The American Institute of CPAs (AICPA) and the Chartered Institute of Management Accountants (CIMA) held the annual Conference on Current SEC and Public Company Accounting Oversight Board (PCAOB) Developments in Washington, D.C., Dec. 6-8, 2021. Overall themes of the conference included:

- Stakeholder roles in fostering high-quality financial reporting
- Environmental, social, and governance (ESG) matters
- Adapting to continuous change

Various stakeholders including preparers, regulators, standard-setters, auditors, users, and others presented the audience with wide-ranging perspectives on these themes.

Focus of the Office of the Chief Accountant

On Dec. 6, 2021, acting SEC Chief Accountant Paul Munter issued a statement on the Office of the Chief Accountant's (OCA) continued focus on high-quality financial reporting in a complex environment. In his statement, he described the OCA's role in the financial reporting system and shared information about its current priorities and its work related to rulemaking activities, oversight of standard-setting, implementation and application of standards, and application of auditor independence requirements. Munter also described the critical role of various stakeholder groups, including accounting standard-setters, preparers, auditors, and audit committees, and he shared observations regarding key areas of focus for each stakeholder group to promote and produce high-quality financial reporting for investors.

Munter identified these elements of high-quality financial reporting: high-quality accounting standard-setting, high-quality implementation and application of those standards, and high-quality audits. He noted that these are necessary to make sure that investors have the information they need to make well-informed investment decisions. To this end, the OCA supports the SEC's rulemaking activities, accounting standard-setting oversight, efforts to promote effective implementation and application of those accounting standards, and PCAOB oversight.

Munter highlighted three rulemaking agenda items that are top of mind for most stakeholders: climate risk disclosures, trading prohibitions under the *Holding Foreign Companies Accountable Act*, and recovery of erroneously awarded compensation. He discussed each of these items in detail, identifying how the SEC and others have been addressing these during the year through guidance, recommendations, and requests.

Munter also said that high-quality financial reporting cannot be achieved without high-quality accounting standards and that one of the OCA's main objectives is to promote the development of such standards. This is accomplished by assisting the SEC in its oversight of Financial Accounting Standards Board (FASB) standard-setting and by promoting high-quality international financial reporting standards (IFRS) and accounting consultations.

Shortly after issuing his statement, on Dec. 6, Munter, with other members of OCA leadership including John Vanosdall and Diana Stoltzfus, both deputy chief accountants, conducted a panel discussion at the AICPA-CIMA conference. The discussion expanded on the themes identified in Munter's prepared statement and provided additional thoughts on topics such as ESG, materiality considerations, consultations, independence, and standard-setting.

Importance of audit committees and auditor independence

Statement on independent audits and effective audit committee oversight
On Oct. 26, 2021, Munter issued a statement addressing the importance of high-quality independent audits and effective audit committee oversight to high-quality financial reporting to investors. He noted the upcoming 20th anniversary of the *Sarbanes-Oxley Act* (SOX) and said that "it is critical for all gatekeepers in the financial reporting ecosystem (auditors, management, and their audit committees) to maintain constant vigilance in the faithful implementation of the requirements of SOX by fulfilling their shared responsibilities to continue to produce high quality financial disclosures that are decision-useful to investors and maintain the public trust in our capital markets. An integral part of the faithful implementation of SOX is for audit firms to remain independent of their audit clients and for audit committees to take ownership of their oversight responsibilities with respect to the independent auditor."

While emphasizing the importance of understanding and applying the general standard of independence, Munter identified auditor independence as "foundational to the credibility of financial statements." He went on to discuss the responsibilities of audit committees, management, and audit firms in considering independence. He warned that as companies pursue access to public markets through new and innovative transactions, and audit firms continue to expand business relationships and nonaudit services, independence must always be considered. Further, Munter highlighted the importance of audit committee oversight of the independent auditor. He stressed that audit committees play a key role in the external independent audit process and that an effective audit committee enhances auditor independence. In his closing, he shared that the gatekeepers should work together and that an effective audit committee overseeing the independent audit is critical to providing high-quality financial information to the capital markets.

Updates to auditor independence rules
On Oct. 16, 2020, the SEC issued final amendments to codify certain staff consultations and update aspects of its auditor independence framework. To address changes in the capital markets and those who participate in them, the amendments update certain aspects of the auditor independence rules so that relationships and services that would not pose threats to an auditor's objectivity and impartiality do not trigger nonsubstantive rule breaches or potentially time-consuming audit committee review of nonsubstantive matters. The rule was effective June 9, 2021.

Additional discussion of the focus of the OCA

Representatives from OCA staff on Dec. 6, 2021, highlighted various topics the staff has addressed in the past year, including:

- Consultation themes such as revenue recognition, special purpose acquisition companies (SPACs), digital assets, and segments
- Independence matters
- International activities, including monitoring of international standard-setting bodies
- Audit matters such as the OCA's role in overseeing the PCAOB and the importance of effective internal control over financial reporting (ICFR)
- Stakeholder engagement

As a reminder of the importance of auditor independence, the OCA staff panel discussion closed with that topic, including advice that auditor independence should not be an afterthought when an entity negotiates the terms of a merger transaction.

Focus of the Division of Corporation Finance

At the AICPA-CIMA conference on Dec. 7, 2021, SEC Division of Corporation Finance (Corp Fin) members, including Corp Fin Director Renee Jones; Lindsay McCord, chief accountant; Craig Olinger, senior adviser to the chief accountant; Sarah Lowe, deputy chief accountant; and Melissa Rocha, deputy chief accountant; provided an overview of recent activities at Corp Fin that affect accounting and reporting for 2021 year-end filings. Topics included:

- Staff challenges, including volume of transactions and filings
- Special purpose acquisition companies
- Climate change disclosure, in particular the staff's recent sample comment letter on the SEC's 2010 climate change interpretive guidance
- Restatements and materiality considerations
- China-based issuers
- Non-GAAP measures and key performance metrics
- Segment reporting
- Spin-off transactions

McCord also provided Corp Fin remarks during the end-of-day question-and-answer session with some observations on the implementation questions the staff fielded on the now effective final rule (from Nov. 19, 2020), "Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information."

Enhanced focus on ESG and climate disclosures

Climate change pledges and disclosures

At a virtual meeting on Dec. 14, 2021, Commissioner Caroline Crenshaw described climate change as a crisis and noted that it will have a substantial impact on the U.S. capital markets. In addressing certain aspects of climate change, she discussed the recent increase in net-zero pledges by public companies and highlighted that in many cases it was unclear how companies would achieve these goals or what information they would need to give investors to evaluate and monitor implementation of these pledges over time. Crenshaw noted that "while net-zero emissions pledges are an important step forward, they underscore the loud, repeated, and sustained calls for decision-useful metrics – metrics calculated using reliable and comparable methodologies that enable investors to decide whether the companies mean what they say." She specifically called out the need for disclosures of political spending as such spending might conflict with companies' net-zero strategies and might further the executives' interests rather than the interests of the investors. Additionally, she noted that linking executive compensation to achieving ESG goals further underscores the need for accurate and reliable climate metrics and decision-useful disclosures.

She concluded with comments on the importance of disclosure of information in the private markets and warned of the risks tied to these markets, where the SEC has less visibility and less oversight.

Commissioner address on ESG and other risks

At a Nov. 16, 2021, conference, Commissioner Crenshaw spoke about ESG matters; digital assets; and internal accounting controls. Crenshaw identified ESG risks as some of the most pressing issues for public companies and investors and said that the reliability of corporate ESG risk disclosures and their potential impact on and connectivity to financial statements is critical. She said that corporate internal controls play a vital role in making sure that ESG risk disclosures are consistent and reliable and reiterated that management is responsible for establishing and maintaining an effective system of internal controls.

In her remarks, she noted that internal accounting controls must be dynamic and evolve over time to consider and respond to changes in the markets. She discussed the importance of assessing whether

existing corporate internal accounting controls are sufficient to provide reasonable assurances that each business and its assets are adequately controlled. Concentrating first on cybersecurity, Crenshaw noted that she was particularly interested in understanding how public companies are responding to cybersecurity intrusions and attacks, which create threats to management's ability to safeguard the company's assets.

Crenshaw shared her thoughts on identifying and measuring climate risk and her interest in understanding how companies are determining whether and how financial statements are affected by climate change risk; how assumptions used to reach these determinations are set, tested, and reevaluated over time; and how any existing disclosures are being formulated. Lastly, she touched on safeguarding digital assets and noted that it is critical for companies to consider, among other things, whether the internal accounting controls frameworks safeguarding these assets are working, how they need to be modified from existing frameworks, and what changes need to be implemented.

Sample comment letter on climate change disclosures

On Sept. 22, 2021, Corp Fin issued a sample comment letter addressing the types of comments staff might offer related to an issuer's climate-related disclosures or lack thereof. While not an exhaustive list, the letter can help registrants consider how current disclosure rules apply to climate-related disclosure.

Stakeholder calls for climate risk disclosures

At the Principles for Responsible Investment "Climate and Global Financial Markets" webinar on July 28, 2021, SEC Chair Gary Gensler addressed the need for climate-related disclosures for public companies and funds to bring transparency to the capital markets.

Gensler said that investors want to understand the climate risks of the companies they invest in or are considering investing in and that these investors are looking for consistent, comparable, and decision-useful disclosures on climate risks. He shared that in response to the SEC's March 2021 statement on climate disclosures, more than 550 unique comment letters were submitted and 75% of these responses supported mandatory climate disclosure rules.

Gensler noted that while companies already are trying to meet the demand for climate risk information, many use generic or boilerplate language that is not decision-useful for investors. Gensler said that both investors and companies would benefit from greater clarity over climate risk disclosures, which is why he has asked SEC staff to develop a mandatory climate risk disclosure rule proposal for consideration by the end of the year. He said that the proposal should consider consistency, comparability, the need for sufficient detail, and both quantitative and qualitative aspects of climate risk. Additionally, he asked SEC staff to consider whether certain metrics for specific industries such as banking should be included.

Additionally, Gensler noted an increase in funds marketing themselves as "green," "sustainable," "low-carbon," and similar but said little information exists to support those claims. He has directed staff to consider whether fund managers should disclose the criteria and underlying data they use in making those claims, including looking at how funds are named.

10 theses for ESG stakeholder discussion

On July 20, 2021, SEC Commissioner Hester Peirce spoke before the Brookings Institution on the SEC's role in ESG disclosures and the complexities and consequences of potential rulemaking. She presented 10 theses to encourage further discussion.

As an alternative to prescriptive ESG rules, Peirce suggested that the SEC could work within its existing regulatory framework to release updated guidance to help issuers consider how the existing disclosure framework elicits ESG disclosure and to address frequently asked questions that arise in connection with the application of the existing disclosure framework. She also suggested working with investment advisers to help investors better understand each adviser's ESG branding and investment practices.

Fund disclosures and diversity disclosures

On July 7, 2021, before the Asset Management Advisory Committee, Chair Gensler and Commissioners Peirce and Crenshaw presented remarks covering ESG, diversity and inclusion, private investments, and technology.

Gensler shared his thoughts on sustainability related to fund disclosures and fund names. He questioned how funds that market themselves using sustainability-related terms support those claims when often the information underlying those claims is not objective, a large range of criteria and sources are used, and no standardized meanings of the sustainability-related terms exist. Gensler said he has asked SEC staff to consider recommendations about whether fund managers should disclose the criteria and underlying data they use. He added that updates to fund disclosures and to naming conventions could bring needed transparency to the asset management industry. He concluded with comments on diversity and inclusion and noted that the asset management industry has a lot of work to do to increase racial and gender diversity; therefore, he has asked SEC staff to consider ways that the SEC can enhance transparency to improve diversity and inclusion practices.

Peirce commented on the pitfalls of ESG standard-setting before addressing diversity and inclusion in U.S. capital markets and her concerns about the committee's draft recommendations. She said that adding government-mandated diversity classifications for the asset management industry might not promote unity and empower people but rather have the opposite effect. Peirce questioned how the SEC would define diversity, how to categorize people with diverse backgrounds, and what do to with those who prefer not to identify, among others. Finally, she said that these recommendations should be open to further debate.

Crenshaw said she agrees that the SEC has a role to play in promoting diversity and inclusion in the asset management industry and she is interested in potential guidance or recommendations that would discourage discrimination by fiduciaries. She mentioned ESG disclosures and the importance that they be consistent, comparable, high quality, and decision-useful. She raised concerns about lack of visibility into the private markets and the need to understand the benefits, risks, and costs of investing in the private markets. She also discussed technology-enabled personalization and how technology can be used to both benefit and harm investors.

IFRS sustainability standards

SEC Commissioner Peirce issued a statement, on July 1, 2021, highlighting her comment letter responding to the IFRS Foundation's proposal to amend its constitution to make possible the creation of an International Sustainability Standards Board to set sustainability standards. In her comment letter, she urges the IFRS Foundation "not to wade into sustainability standard-setting because doing so would (i) improperly equate sustainability standards with financial reporting standards, (ii) undermine the Foundation's current important, investor-centered work, and (iii) raise serious governance concerns." Peirce warns, "We must be careful not to compromise accounting standard-setting in an effort to achieve objectives other than high-quality financial reporting," as accounting and sustainability standards are fundamentally different from one another.

SEC chair ESG remarks

On June 23, 2021, at London City Week, SEC Chair Gensler presented prepared remarks on public company disclosure, market structure, and transparency resulting from ESG initiatives. His remarks on public company disclosure focused on his requests that SEC staff make recommendations on and consider the following:

- Mandatory company disclosures on climate risk and human capital to address the need for consistent, comparable, and useful investment decision-making information
- Climate risk governance, strategy, and risk management, including specific metrics that might be relevant
- Potential requirements for companies that make forward-looking climate commitments
- Ways that funds are marketing themselves to investors as sustainable, green, and focused on ESG matters, and what factors support those claims
- Human capital disclosures that might include metrics such as workforce turnover, skills and development training, compensation, benefits, workforce demographics including diversity, and health and safety

SEC commissioner discussion of climate, ESG matters, and the board of directors

SEC Commissioner Allison Herren Lee presented the keynote address at the 2021 Society for Corporate Governance conference on June 28, 2021. She addressed the important role corporate directors play in overseeing climate and ESG issues. Lee discussed:

- Putting ESG matters in context in the recent proxy season. Lee described actions taken during the most recent proxy season and highlighted shareholder proposals related to climate and racial equity and how the increase in such activity shows the importance of addressing and integrating climate and ESG issues into decision-making, risk management, and corporate initiatives.
- Understanding ESG and board obligations. Lee noted that "boards increasingly have oversight obligations related to climate and ESG risks – identification, assessment, decision-making, and disclosure of such risks."
- Mitigating ESG risks and maximizing ESG opportunities. Lee identified physical, transition, regulatory, reputational, and human capital risks and said enhancing board diversity, increasing board expertise, and inspiring management success present opportunities for boards to position themselves as ESG leaders.

Sustainability of ESG rules

On June 22, 2021, SEC Commissioner Elad Roisman spoke at the National Investor Relations Institute's virtual conference. He focused on three questions, including:

1. "What precise items of 'E,' 'S,' and 'G' information are investors not getting that are material to making informed investment decisions?
2. "If we were able to identify the information investors need, how would the SEC come up with 'E' and 'S' disclosure requirements – now, and on an ongoing basis? What expertise do we need?
3. "If the SEC were to incorporate the work of external standard-setters with respect to new ESG disclosure requirements: how would the agency oversee them – in terms of governance, funding, and substantive work product – on an ongoing basis? And what kind of new infrastructure would be required inside the SEC and at the standard-setters themselves?"

In addressing these questions, Roisman noted that determining who the investors are and understanding from those investors what ESG information is missing from the markets is vital. He also asked how the SEC would provide one list of ESG disclosures for companies that could satisfy the differing and evolving demands for ESG information. Roisman noted that any new disclosure requirements should focus on what information is material to an investment decision. He also raised questions about how the SEC will acquire and maintain expertise over environmental and social areas to develop and oversee disclosure requirements when information in these areas quickly changes. He noted concerns over how the standards would be updated over time. Roisman said that considering these questions will help the SEC meet the challenging task of creating ESG rules that are sustainable.

Potential costs of ESG disclosures

On June 3, 2021, before the ESG Board Forum, SEC Commissioner Roisman presented a speech on ESG disclosures and the potential costs related to requiring specific disclosures. After sharing reservations regarding the SEC issuing ESG disclosure requirements because it would be difficult to standardize such requirements to provide meaningful and not misleading information, he raised several questions that the SEC would need to address when crafting new rules over ESG disclosures. He then concentrated on ways to mitigate various costs and difficulties of new ESG disclosure requirements.

Roisman first identified the importance of minimizing costs and burdens related to understanding what investors want. He warned of the foreseeable costs not only of obtaining and presenting new information but also of increased liability related to such new disclosures. Roisman stated that if the costs are foreseeable they can be addressed beforehand as the new rules are developed.

Roisman then addressed ways to tailor ESG disclosure requirements including:

- Scaling the disclosures for public issuers based on size
- Providing flexibility in sources and methodologies
- Considering safe harbors for companies that are making an earnest effort to provide this new information
- Considering having the disclosure information furnished to instead of filed with the SEC
- Extending the implementation period and having a phased-in approach

In closing, Roisman said, "any new ESG disclosure rules will inevitably come with costs. Especially since such disclosure would involve information that is based on uncertain underlying assumptions, or is difficult to calculate, the Commission should be particularly careful to ensure that (1) investors understand the limitations of the information disclosed and (2) companies can actually provide such information without incurring undue costs and burdens."

Materiality considerations about ESG disclosures

On May 24, 2021, SEC Commissioner Lee presented keynote remarks at the 2021 ESG Disclosure Priorities Event hosted by the American Institute of CPAs & the Chartered Institute of Management Accountants, Sustainability Accounting Standards Board, and the Center for Audit Quality. Her remarks concentrated on potential misconceptions about materiality specifically related to ESG and required disclosures.

She explained that materiality is a fundamental proposition in the securities laws and in the capital markets and disclosure is focused on providing information that is important to reasonable investors. In her remarks, Lee identified four misconceptions about materiality specifically related to ESG**.** Lee closed with a warning not to believe these misconceptions. She shared her hope that the misconceptions can be overcome as the deliberations continue on how best to craft a rule proposal on climate and ESG risks and opportunities.

SEC chair answers to ESG questions

While hearing testimony on market volatility, the House Committee on Financial Services on May 6, 2021, questioned SEC Chair Gensler about the increased focus on climate-related disclosures and updates to climate disclosure guidance. In response, Gensler said that the staff has been asked to prepare recommendations based on public input about what climate-related disclosures and climate risk areas are important to investors to help bring consistency and comparability to such disclosures.

Determinations about guidance will be made through those recommendations; economic analysis; information gathered by the ESG task force; and other critical input from the public, including responses to the request for public comment on climate change disclosures issued by former acting Chair Lee. Comments on that request were due in June 2021. Based on analysis of the information gathered, the SEC will prepare a proposal for public comment.

SEC commissioner remarks on ESG

On April 28, 2021, SEC Commissioner Peirce provided remarks before the International Swaps and Derivatives Association Derivatives Trading Forum on Regulatory Change. Peirce spoke about the enhanced focus on ESG reporting. Peirce warned the audience that it must learn from the London Interbank Offered Rate (LIBOR) situation before rushing into the ESG space. She said that LIBOR lacked precision and that we are diving right into adopting ESG measures that portray an impression of precision but might not be as precise with such varying approaches. She noted that it is very difficult to measure how green a particular investment, issuer, or transaction is, and numerous factors need to be considered when making capital decisions. She further stressed caution and the need to proceed with care as ESG strategies are implemented, as there is a responsibility to shareholders and customers not to embrace approaches that will harm the capital markets, the financial system, or the planet.

Risk alert on ESG investing

The SEC Division of Examinations released, on April 9, 2021, a risk alert, "The Division of Examinations' Review of ESG Investing," detailing observations from recent exams of investment advisers, registered investment companies, and private funds offering ESG products and services. The alert is intended to highlight risk areas and assist firms in developing and enhancing their compliance practices. The alert notes that entities approach ESG investing in various ways. It details observations of deficiencies and internal control weaknesses related to ESG investing from the examinations and provides observations of effective practices. The alert also says that firms should present disclosures that are clear, precise, and tailored to firms' specific approaches to ESG investing and that align with the firms' actual practices.

Commissioner statement on ESG risk alert

SEC Commissioner Peirce issued, on April 12, 2021, a statement following the release of the staff ESG risk alert on April 9. Peirce says, "Firms claiming to be conducting ESG investing need to explain to investors what they mean by ESG and they need to do what they say they are doing." She says that the risk alert requires some context and should not be interpreted as a sign that ESG investment strategies are a unique consideration for examiners. As with any other investment strategy, the SEC examiners will be looking for consistency between claims and practices and not assessing whether a firm's strategy is a good one and not attempting to insert its own views in the investment advisory process.

In addition, Peirce notes that the risk alert should be considered with the SEC's two recent proxy voting interpretive releases, and she clarifies that firms do not need a special set of policies and procedures for ESG or for any investment strategy. Firms' policies and procedures should be designed around the investment strategies the firm uses, and the risk alert does not create new obligations for registrants. Peirce says that the staff's role is to understand whether firms are adhering to their own ESG claims.

Peirce concludes that while the risk alert raises questions, she hopes that it will be a useful tool for sellers of ESG products and services and that it will help protect buyers.

Acting SEC chair directive on climate-related disclosure

Public company audit committees and preparers should be aware in preparing their disclosure documents that on Feb. 24, 2021, acting SEC Chair Lee announced she was directing Corp Fin staff to enhance its focus on climate-related disclosures in public company filings. She said Corp Fin staff should "review the extent to which public companies address the topics identified in the 2010 guidance, assess compliance with disclosure obligations under the federal securities laws, engage with public companies on these issues, and absorb critical lessons on how the market is currently managing climate-related risks." Insights learned from this review process will be used by Corp Fin to update the 2010 guidance.

On March 15, 2021, Lee announced a request for public comment on climate change disclosures to further inform the SEC's policymaking. The SEC posed 15 questions. Comments were due June 13, 2021.

In response to the request for comment, the SEC received more than 5,700 comment letters. Of the 5,700, approximately 300 were unique and 5,400 represented variations of four different form letters. The SEC staff also documented approximately 30 meetings with stakeholder groups over the previous three months regarding the request.

Commissioners on enhanced focus on climate and ESG

SEC Commissioners Peirce and Roisman issued, on March 4, 2021, a public statement addressing the recently issued statements and press releases on ESG matters. In their statement, Peirce and Roisman contemplate the meaning of the enhanced focus on climate and ESG-related matters and provide some thoughts on the recent announcements.

Regarding the statements from acting Chair Lee in her directive to Corp Fin, the commissioners say they believe that – given the focus of Corp Fin on reviewing companies' disclosures, assessing their compliance with disclosure requirements under the federal securities laws, and engaging with issuers on climate change and ESG issues – the initiative is a continuation of the work already being conducted and not a plan to assess disclosures against any new standards or expectations. With regard to

updating the SEC's 2010 guidance, Peirce and Roisman say they do not believe that a plan exists to issue guidance establishing more specific line items or changing the SEC's principles-based approach to a prescriptive one.

The announcement of the 2021 examination priorities highlights that the SEC will enhance its focus on climate and ESG-related risks; however, the identified areas do not specifically include a climate or ESG focus. The commissioners note that the risk-based reviews of compliance with existing statutes and regulations will touch on climate and ESG-related risks given the current environment; however, the review will have a broader focus.

The commissioners also said that the purpose of the newly created Climate and ESG Task Force is not clear, as currently the Division of Enforcement identifies, investigates, and brings actions against those who violate the SEC's laws and rules and no new standards related to climate and ESG have been introduced.

On March 19, 2021, Peirce and Roisman provided, in prepared statements at the SEC's Asset Management Advisory Committee, additional perspectives on ESG matters.

Climate and ESG enforcement task force

The SEC announced, on March 4, 2021, the creation of a Climate and ESG Task Force in the Division of Enforcement. The task force, led by Kelly L. Gibson, the acting deputy director of enforcement, will develop initiatives to identify misconduct related to ESG issues. Initially, the task force will focus on identifying material gaps or misstatements in issuers' disclosure of climate and ESG risks under existing rules and will coordinate with other SEC resources to identify potential violations. In addition, the task force will assess and pursue tips, referrals, and whistleblower complaints on issues related to ESG, and it will provide expertise to teams working on ESG-related matters.

Remarks on ESG disclosure

Acting Corp Fin Director John Coates shared observations on ESG disclosure at the 33rd annual Tulane Law Institute on March 11, 2021, including:

- Considerations for an effective ESG disclosure system
- Costs of not having ESG disclosure requirements
- Mandatory versus voluntary disclosure
- Benefits of having a global ESG reporting framework

Coates believes policymakers, including the SEC, should consider these issues when debating ESG disclosures, and he remarked the SEC's approach to ESG disclosures should be both "adaptive and innovative."

SEC climate and ESG resource page

The SEC has created a new page addressing the SEC's response to climate and ESG risks and opportunities. The page brings together all of the recent climate- and ESG-related actions in one location.

Crowe ESG resource

As investors and other stakeholders increasingly focus on ESG factors as part of their investment decisions, some entities are seeking a greater understanding of ESG disclosures. Crowe has released an article, "Got ESG? Current Developments in ESG Disclosure," to provide entities with information about ESG disclosure developments.

Crowe has also created a resource page, "Resources for Your ESG Strategy," to bring together various sources and articles and provide knowledge regarding understanding ESG and ESG strategy considerations.

SEC coronavirus response

The SEC maintains a COVID-19 response page, which describes how the SEC is addressing the impact of COVID-19 through maintaining SEC operations continuity; monitoring markets and engaging with

market participants; providing guidance and targeted regulatory assistance and relief, enforcement, examinations, and investor education; and extending comment periods for certain pending actions and rules. The page includes links to current SEC resources and guidance related to COVID-19.

From the top

Testimony before House committee

Oct. 5, 2021, SEC Chair Gensler testified before the U.S. House of Representatives Committee on Financial Services. Gensler addressed market structure, predictive data analytics, disclosures, and funds and investment management. He closed with comments on enforcement and examinations and resources at the SEC.

Gensler discussed the Treasury market, non-Treasury fixed income markets, equity markets, security-based swaps, and crypto asset markets and described the market structure-based projects that he has asked SEC staff to review. These projects include enhancing resiliency and competition in the Treasury market, reconsidering some initiatives on Treasury trading platforms, bringing greater efficiency and transparency to the non-Treasury fixed income markets, and updating the SEC's rules to address new technologies. He described the rules going into effect this year and next year for security-based swaps and the rules in process for the registration and regulation of security-based swap execution facilities. He also identified the need for additional investor protections in crypto finance, issuance, trading, and lending and the need to work with other regulators on this.

After touching on the potential conflicts and systemic risk that might arise with predictive data analytics, Gensler spoke about the importance of consistent, comparable, and decision-useful disclosures related to climate risk, human capital, and cybersecurity. He also discussed SPACs and his request to staff for recommendations on enhancing SPAC disclosures. Gensler provided testimony related to enhancing disclosures with regard to how Chinese companies issue securities in the U.S. Finally, he mentioned tightening insider trading rules.

While discussing funds and investment management, he highlighted the increasing number of funds that market themselves as "green," "sustainable," "low-carbon," and similar. Gensler noted the importance of understanding what supports those claims and shared that the SEC staff is developing a proposal on cybersecurity risk governance, which will address issues such as cyber hygiene and incident reporting.

Testimony on SEC's unified rulemaking agenda

On Sept. 14, 2021, SEC Chair Gensler testified before the Senate Committee on Banking, Housing, and Urban Affairs. His testimony focused on current work of SEC staff on areas identified in the most recent SEC rulemaking agenda including:

- Market structure (Treasury, non-Treasury fixed income, equity, security-based swaps, and crypto asset markets)
- Predictive data analytics
- Issuers and issuer disclosure (including climate risk, human capital, cybersecurity, SPACs, China, and 10b5-1 plans)
- Funds and investment management

Gensler concluded his remarks with observations from the SEC's enforcement and examinations activities.

Competition and regulatory reform at the PCAOB

On Sept. 9, 2021, the SEC's Investor Advisory Committee (IAC) met to discuss various matters including consideration of audit firm competition and regulatory reform at the PCAOB. The discussion of competition and regulatory reform included panelists representing various stakeholders in the financial reporting ecosystem. Panelists debated how audit opinion customers (that is, audit committees) and consumers (that is, investors) receive and use information about audit quality as well as how communication of that information could be changed or improved to meet various stakeholder objectives. The discussion also focused on the PCAOB's current role in fostering audit quality and how

that role might evolve in the future in light of the ever-changing landscape of stakeholder needs and technology. Jurisdictional differences in audit regulatory regimes also arose as a topic in the discussion.

The IAC meeting also included a panel discussion of investor protection in light of the behavioral design of certain online trading platforms, and the IAC also voted to provide the SEC with certain recommendations regarding SPACs and Rule 10b5-1 trading plans.

Prepared remarks of SEC Chair Gensler, Commissioners Peirce and Roisman, and certain panelists are available.

Testimony on resources and trends

SEC Chair Gensler appeared before the Subcommittee on Financial Services and General Government of the U.S. House Appropriations Committee on May 26, 2021, to provide testimony on trends in capital markets affecting SEC resources, the impact of the pandemic on the SEC's work, and other SEC initiatives. Gensler shared his opinion on the vast scope of the SEC, the significant growth in the capital markets, and the lack of growth in the size of the SEC and its resources. Gensler emphasized that the SEC needs to ensure it has the resources to protect investors accessing the capital markets, and he identified the following five key capital market trends that will affect SEC resource needs:

- Significant increases in initial public offerings and special purpose acquisition companies
- Substantial growth in the number of private funds
- Growth in the use of crypto assets, which are highly volatile and speculative
- New business models and technologies related to fintech
- Increasing reliance on data analytics

Gensler provided details to give a better picture of how each of these key capital market trends is currently affecting and will affect SEC resources and how each is affecting the capital markets. Additionally, Gensler identified these four initiatives affecting the SEC:

- Rules on security-based swaps that became effective in 2021
- Implementation of Regulation Best Interest
- Consideration of economic analysis and input from the public on disclosures
- Addressing the transition from LIBOR

In closing, Gensler repeated that the SEC is working with fewer resources than it had five years ago and noted that he looks "forward to working with Congress on additional resources so the SEC can stay apace of these important trends."

Statement on investor protection related to developments in China

On July 31, 2021, SEC Chair Gensler released a public statement addressing actions he directed the staff to take in response to recent regulatory developments in China.

Policy matters

SEC regulatory agenda and commissioner perspectives

In December 2021, the SEC announced updates to its regulatory agenda, which lists short- and long-term regulatory actions the SEC plans to take. The revised agenda provides updated forecasts for potential rulemaking action on various topics including climate change, human capital, board diversity, and cybersecurity governance. Commissioners Roisman and Peirce communicated alternative perspectives on certain aspects of Chair Gensler's regulatory agenda on Dec. 13.

Report on market volatility

The SEC staff issued, on Oct. 18, 2021, a report titled, "Staff Report on Equity and Options Market Structure Conditions in Early 2021." The report provides a description of the U.S. market structure and securities regulatory framework and examines what happened with GameStop Corp. stock, a "meme stock," which experienced dramatic increases in its share price in January 2021. The report examines trading activity of GameStop stock, increasing individual investor participation, short selling, and trading restrictions, among other topics.

The report proposes that "meme stock" events present an opportunity to reflect on the market structure and regulatory framework and identifies the following areas for potential study in the interests of protecting investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation:

- Forces that might cause a brokerage to restrict trading
- Digital engagement practices and payment for order flow
- Trading in dark pools and through wholesalers
- Short selling and market dynamics

Also on Oct. 18, Gensler released a statement on the staff report, and Peirce and Roisman released a separate statement. Gensler highlighted the importance of furthering efforts to make equity markets as fair, orderly, and efficient as possible. Saying they "look forward to a robust policy discussion," Peirce and Roisman stated, "We always should be on the lookout for ways to improve our rules and our markets." However, they noted that "it does not appear that many conclusions can be drawn from the data [in the report]."

SEC commissioner remarks on risks

On Sept. 24, 2021, before the "Symposium on Building the Financial System of the 21st Century" hosted by the Program on International Financial Systems and Harvard Law School, Commissioner Crenshaw presented remarks on assessing risks. She warned, "In times of consistent and positive stock market returns, we should not be lulled into complacency," and said market participants and regulators must continually be aware of and assess risks. Crenshaw added, "the difficulty of anticipating the unknown does not relieve us of our responsibility to be proactive."

Crenshaw noted that risks are both from within the financial system and external. Related to risks within, Crenshaw discussed riskier investments with higher yields, swaps, and options trading. She said, "Effective compliance and risk management at financial institutions doesn't just protect those institutions and their shareholders, it also helps make financial markets more resilient." She shared that some of these investments and strategies are very risky and can result in significant losses. For external risks, Crenshaw concentrated her remarks on climate, cybersecurity, and geopolitical risks. She further highlighted actions the SEC is taking relating to these risks and stressed the need for disclosures.

MOU with European Central Bank on cooperation with security-based swap entities

On Aug. 16, 2021, the SEC and the European Central Bank signed a Memorandum of Understanding (MOU) to consult, cooperate, and exchange information in connection with the supervision, enforcement, and oversight of certain security-based swap dealers and major security-based swap participants that are registered with the SEC and supervised by the European Central Bank.

The MOU is intended to facilitate the SEC's oversight of all SEC-registered security-based swap entities in European Union (EU) member states participating in the Single Supervisory Mechanism (SSM), which is the system of banking supervision in the EU. It is composed of the European Central Bank and the relevant national competent authorities of participating EU member states.

The SEC describes in the release that the MOU "will also support the SEC's oversight of the operation of substituted compliance orders that the Commission has issued for security-based swap entities in France and Germany, as well as any future substituted compliance orders for such firms in other EU Member States that participate in the SSM."

Security-based swaps regulatory activities

SEC Chair Gensler discussed the SEC's regulatory activities regarding security-based swaps at the American Bar Association Derivatives and Futures Law Committee virtual midyear meeting on July 21, 2021.

Gensler first discussed the legislation adopted in response to the 2008 financial crisis, which was meant to reduce risk related to security-based swaps by requiring dealers to register with the SEC. Registered dealers needed to have certain back-office controls and adequate cushions against losses, through both their capital levels and their customer margin. Focusing on reducing risk, newer registration requirements include new counterparty protections and requirements for capital and margin, internal risk management, supervision and chief compliance officers, trade acknowledgment and confirmation, and recordkeeping and reporting procedures. Security-based swap dealers and major security-based swap participants began registering with the SEC Nov. 1, 2021.

In addition, Gensler discussed the relationship between security-based swaps and financial technology, including the topic of crypto assets. Gensler said, "There are initiatives by a number of platforms to offer crypto tokens or other products that are priced off of the value of securities and operate like derivatives." He cautioned, "It doesn't matter whether it's a stock token, a stable value token backed by securities, or any other virtual product that provides synthetic exposure to underlying securities. These platforms – whether in the decentralized or centralized finance space – are implicated by the securities laws and must work within our securities regime." He said SEC rules apply to security-based swaps.

LIBOR transition

Statement on LIBOR transition

The SEC, on Dec. 7, 2021, published "SEC Staff Statement on LIBOR Transition – Key Considerations for Market Participants" to remind investment professionals of their obligations when recommending LIBOR-linked securities and to remind companies and issuers of asset-backed securities of their disclosure obligations related to the LIBOR transition. This statement follows previous staff statements addressing other aspects of the approaching LIBOR transition. This statement addresses:

- Background and general considerations for market participants
- Broker-dealer registrants: recommendations to retail customers
- Broker-dealer registrants: municipal securities underwriting and sales to customers
- Registered investment advisers and funds
- Disclosure considerations for public companies and asset-backed securities issuers

SEC chair LIBOR transition remarks

On Sept. 20, 2021, Chair Gensler spoke on LIBOR to the "SOFR Symposium" hosted by the Fed's Alternative Reference Rates Committee. He gave a short history of LIBOR transition and reiterated his June 11, 2021, message that the BSBY, championed by certain commercial banks as an alternative to LIBOR, might have the same conceptual perils as LIBOR. In conclusion, he shared that he agreed with the committee that the Secured Overnight Financing Rate (SOFR) is a preferable alternative rate.

Omnibus statement on LIBOR transition and potential risks

On July 12, 2019, SEC staff from multiple divisions and offices published a statement on LIBOR transition that encourages market participants to proactively manage their transition away from LIBOR. The statement identifies several areas that warrant increased attention during the transition period and provides guidance on certain items. Areas addressed in the statement include:

- Identification of existing contracts that extend past 2021 to determine an entity's exposure to LIBOR
- Consideration of whether future contracts should reference an alternative rate to LIBOR or include effective fallback language

- Guidance for how registrants might respond to other business risks associated with the discontinuation of LIBOR such as those related to strategy, products, processes, and information systems
- Questions to consider that will assist an entity in understanding and mitigating the risks related to LIBOR transition
- Potential alternative reference rates
- Guidance from several SEC divisions on responding to risks from the impact of LIBOR discontinuation

It is expected that parties reporting information used to set LIBOR will stop doing so after 2021.

The SEC staff warns, "For many market participants, waiting until all open questions have been answered to begin this important work likely could prove to be too late to accomplish the challenging task required." Chair Jay Clayton also remarked at the 2019 AICPA conference that "[h]ope is not a strategy" with respect to LIBOR transition. Corp Fin staff mentioned at the 2020 AICPA conference that where material, disclosure related to LIBOR transition will be a staff focus area.

SEC chair address on LIBOR

Chair Gensler discussed LIBOR transition in his June 11, 2021, remarks to the Financial Stability Oversight Council (FSOC). He encouraged the FSOC to consider his concerns regarding the robustness of the Bloomberg Short-Term Bank Yield Index (BSBY), which is a rate that "a number of commercial banks are advocating as a replacement for LIBOR." He remarked that he believed BSBY has many of the same flaws as LIBOR and cautioned against the pitfalls of allowing BSBY as a replacement rate. Gensler supports as a preferable alternative to LIBOR the SOFR, which is based on a nearly trillion-dollar market.

SEC commissioner address on LIBOR

On April 28, 2021, SEC Commissioner Peirce provided remarks before the International Swaps and Derivatives Association Derivatives Trading Forum on Regulatory Change. Among other topics, Peirce spoke about upcoming changes related to the discontinued use of LIBOR.

Peirce shared her thoughts on the importance of embracing changes and warns of consequences of not addressing changes. As LIBOR is set to be discontinued, Peirce, referencing others' statements, warns that LIBOR discontinuation "could have a significant impact on the municipal securities market and may present a material risk for many issuers of municipal securities and other obligated persons." She said that trillions of dollars of contracts still reference LIBOR, that many of these contracts lack fallback language, and that changing to alternative reference rates creates a diverse mix of significant challenges. She noted that the SEC is continuing to closely follow developments in this area and is working with other regulators and entities to help ensure steps are being taken to address this challenge. She mentioned the SEC risk alert covering LIBOR transition readiness and the work that the SEC, in conjunction with other regulators, has been doing to address the transition from LIBOR. Peirce also discussed proposed legislation that would insert a fallback into contracts that do not include one, and the concern that such legislation would override private contracts.

From the Office of the Chief Accountant

"Spring-loaded" compensation awards to executives

On Nov. 29, 2021, SEC staff issued Staff Accounting Bulletin No. 120, which outlines new interpretive guidance on "spring-loaded" awards to executives, and estimating the fair value of share-based payment transactions under Accounting Standards Codification (ASC) Topic 718, "Compensation – Stock Compensation," when an entity has not yet released known and material nonpublic information. Spring-loaded awards are share-based payments granted shortly before the release of market-moving information, such as an earnings release with better-than-expected results or the disclosure of a significant transaction. SEC staff observes that spring-loaded awards should receive particular scrutiny from those charged with governance over a public entity's compensation and financial reporting. In

addition, any incremental value related to the anticipated release of material nonpublic information should be considered as an entity measures compensation cost for such awards.

The new guidance addresses whether adjustments to the current share price or the expected volatility assumption are appropriate when using a measurement method based on fair value for share-based payment transactions. The staff provides examples of when adjustments might be necessary and also offers reminders of an entity's corporate governance and disclosure obligations as well as the need to maintain effective internal control over financial reporting.

Option to delay GAAP provisions under the CARES Act

On April 3, 2020, the chief accountant of the SEC issued a statement noting the *Coronavirus Aid, Relief, and Economic Security Act* (CARES Act) provides the option to temporarily defer or suspend the application of two provisions of GAAP and would be in accordance with GAAP. The two provisions of the act are Section 4013 and Section 4014, "Optional Temporary Relief From Current Expected Credit Losses."

As such, eligible registrants could elect to take the delay. Registrants had to make the election for the first quarter. During the delay, those registrants continued to use the incurred loss model for the allowance for loan and lease losses (ALLL) for each quarter. The delay was slated to end the earlier of the termination of the national emergency or Dec. 31, 2020. Regardless of when the national emergency ends, those banks were slated to adopt the current expected credit loss (CECL) model in the fourth quarter of 2020, retrospective to Jan. 1, 2020. The result would have been all calendar year registrants reflecting CECL in their 2020 Form 10-K.

On Dec. 27, 2020, H.R. 133, *Consolidated Appropriations Act, 2021*, was signed into law and extends certain provisions of the CARES Act. Section 4013 of the CARES Act provided temporary relief from troubled debt restructuring (TDR) and is amended by Division N, Section 540 of H.R. 133, by extending the end date from Dec. 31, 2020, to the earlier of Jan. 1, 2022, or 60 days after the date on which the COVID-19 national emergency terminates. It also adds specific reference to insurance companies in addition to the previously covered financial institutions.

Division N, Section 541 of H.R. 133 extends CARES Act Section 4014, which provided optional temporary relief from CECL guidance. Under this extension, insured depository institutions, bank holding companies, and their affiliates would not be required to adopt FASB Accounting Standards Update (ASU) 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments," before the earlier of the first day of the entity's fiscal year that begins after the date on which the COVID-19 national emergency terminates or Jan. 1, 2022.

After the CARES Act was enacted on March 27, 2020, the SEC staff clarified that once the deferral was elected by a registrant, Dec. 31, 2020, adoption of CECL was required, retrospective to Jan. 1, 2020 (ignoring an early termination of the national emergency). Under the amendments, a registrant electing the delay under the CARES Act was further delayed until Jan. 1, 2022, effective as of Jan. 1, 2022 (absent an early termination of the national emergency). With regard to the amendments to Section 4014, the SEC staff indicated it would not object to a registrant early adopting on Dec. 31, 2020, retrospective to Jan. 1, 2020, or Jan. 1, 2021, effective as of Jan. 1, 2021.

From the Division of Corporation Finance

Capital formation, investor protection, and rulemaking

Rule proposals

Proposed amendments to share repurchase disclosures and reporting

On Dec. 15, 2021, the SEC issued proposed amendments to its rules covering disclosure about an issuer's repurchases of its equity securities, commonly known as share buybacks. The proposed rules would apply to issuers that repurchase securities registered under Section 12 of the *Securities Exchange Act of 1934*, including foreign private issuers and certain registered closed-end funds. Under

the proposed amendments, issuers would be required to complete and provide a new Form SR before the end of the first business day following the day the issuer executes a share repurchase. This new form would include disclosure of the class of securities purchased, total amount purchased, average price paid, and the aggregate total amount purchased on the open market in reliance on the safe harbor in *Exchange Act* Rule 10b-18 or pursuant to a plan that is intended to satisfy the affirmative defense conditions of *Exchange Act* Rule 10b5-1(c).

Additionally, the proposed rules would require an issuer to disclose:

- The objective or rationale for the share repurchases and the process or criteria used to determine the amounts of repurchases
- Any policies and procedures relating to purchases and sales of the issuer's securities by its officers and directors during a repurchase program, including any restriction
- Whether the issuer is making its repurchases pursuant to a plan that it intends to satisfy the affirmative defense conditions of *Exchange Act* Rule 10b5-1(c) and/or the conditions of the *Exchange Act* Rule 10b-18 nonexclusive safe harbor

Comments are due 45 days after publication in the Federal Register.

Proposed amendments to insider trading plans and related disclosures

The SEC, on Dec. 15, 2021, issued a proposal, "Rule 10b5-1 and Insider Trading," for public comment. This proposal includes amendments to Rule 10b5-1 under the *Securities Exchange Act of 1934* to enhance disclosure requirements and investor protections against insider trading. The proposal includes updates to Rule 10b5-1(c), which provides an affirmative defense to insider trading for parties that frequently have access to material nonpublic information, including corporate officers, directors, and issuers.

The amendments would update the requirements for the affirmative defense by imposing a cooling-off period before trading could commence under a trading plan, prohibiting overlapping trading plans, and limiting single trade plans to one trading plan in any 12-month period. Additionally, the proposal would require directors and officers to furnish written certifications that they are not aware of any material nonpublic information when they enter into the plans. New disclosures about an issuer's policies and procedures related to insider trading and practices around the timing of options grants and the release of material nonpublic information also would be required. A new table would report any options granted within 14 days of the release of material nonpublic information and the market price of the underlying securities on the trading days before and after the disclosure of the material nonpublic information.

Comments are due 45 days after publication in the Federal Register.

Proposed amendments to money market fund rules

On Dec. 15, 2021, the SEC proposed amendments to certain rules governing money market funds under the *Investment Company Act of 1940*. As the concerns over the economic impact of the pandemic escalated in March 2020, many investors reallocated their assets, resulting in large outflows from prime and tax-exempt money market funds and creating stress on short-term funding markets. The proposed amendments address concerns about such money market funds, including concerns about redemption costs and liquidity, and are intended to decrease the chances of runs on such funds in times of stress.

The proposed amendments would:

- Increase liquidity requirements for money market funds to provide a more substantial liquidity buffer in the event of rapid redemptions
- Remove provisions permitting or requiring a money market fund to impose liquidity fees or to suspend redemptions through a gate when a fund's liquidity drops below an identified threshold
- Require institutional prime and institutional tax-exempt money market funds to implement swing pricing policies and procedures that would require redeeming investors to bear the liquidity costs of their redemptions under certain circumstances
- Change certain reporting requirements to improve the availability of information about money market funds

Comments are due 60 days after publication in the Federal Register.

Proposed rules over security-based swaps transactions and positions

The SEC, on Dec. 15, 2021, proposed rules related to security-based swap transactions and positions. The proposal includes the following new rules:

- Rule 9j-1 would prohibit fraudulent, deceptive, or manipulative conduct in connection with all transactions in security-based swaps.
- Rule 15Fh-4(c) would prohibit personnel of a security-based swap entity from taking any action to coerce, mislead, or otherwise interfere with the security-based swap entity's chief compliance officer.
- Rule 10B-1 would require any person, or group of persons, who owns a security-based swap position that exceeds the threshold amount included in the rule to publicly report to the SEC information required by Schedule 10B on the SEC's EDGAR filing system.

Comments are due 45 days after publication in the Federal Register.

Proposed changes to increase securities lending market transparency

The SEC, on Nov. 18, 2021, published a proposed rule on the reporting of securities loans. The rule is intended to strengthen the transparency and efficiency of the securities lending market. It would require lenders of securities to provide the material terms of securities lending transactions to a registered national securities association. That association would then make available to the public certain information concerning each transaction and aggregate information on securities on loan and available to loan.

Concurrent with the release of this proposal, Chair Gensler released a statement noting that securities lending and borrowing is an important part of the U.S. market structure and that the public benefits from transparency and competition. Gensler stated, "it's important that market participants have access to fair, accurate, and timely information," and he said, "this proposal would bring securities lending out of the dark."

Comments were due Jan. 7, 2022.

Proposed amendments to proxy voting advice rules

On Nov. 17, 2021, the SEC approved for public comment proposed amendments to its rules governing proxy voting advice. First, the SEC is proposing to rescind conditions to the availability of two exemptions from the proxy rules' informational and filing requirements on which proxy voting advice businesses often rely. Second, the proposed amendments would rescind the 2020 changes made to the proxy rules' liability provision. Comments were due Dec. 27, 2021.

Commissioners Crenshaw, Lee, Roisman, and Peirce issued statements on the proxy voting proposal.

Proposed *Securities Act* amendments

The SEC, on Dec. 22, 2020, proposed an amendment to Rule 144 under the *Securities Act of 1933.* The proposed amendment would revise the holding period determination for securities acquired upon the conversion or exchange of market-adjustable securities that meet certain criteria as defined in the amendment. The proposal is designed to reduce the risk of unregistered distributions in connection with sales of those securities. Related to this amendment, the SEC also proposed amendments to update and simplify the Form 144 filing requirements.

Under the current Rule 144, securities acquired solely in exchange for other securities of the same issuer are deemed to have been acquired at the same time as the securities surrendered for conversion or exchange. Under the proposed amendments, the holding period for the underlying securities acquired upon conversion or exchange of certain market-adjustable securities would not begin until conversion or exchange, thereby requiring that a purchaser would need to hold the underlying securities for the applicable Rule 144 holding period before reselling them under Rule 144.

The proposed amendments to Form 144 would mandate electronic filing of the form, remove the requirement to file a Form 144 with respect to sales of securities issued by companies that are not subject to *Exchange Act* reporting, and revise the filing deadline to match the Form 4 filing deadline.

Comments were due March 22, 2021.

Proposed changes to framework for securities offerings and sales to workers

On Nov. 24, 2020, the SEC proposed amendments to Rule 701 of the *Securities Act of 1933* as well as to Form S-8, the *Securities Act* registration statement for compensatory offerings by reporting issuers. Rule 701 provides an exemption from registration for the issuance of compensatory securities by nonreporting issuers.

Additionally, in a companion release, the SEC proposed rules to permit, on a temporary basis and subject to certain conditions, an issuer to provide equity compensation to certain workers who provide services available through the issuer's technology-based marketplace platform.

Significant changes in compensatory offerings and composition of the workforce have happened since the SEC last amended Rule 701 and Form S-8. The proposed amendments are designed to modernize the framework for compensatory securities offerings, allowing employees and other workers to receive equity compensation from their company while maintaining important investor protections.

Comments on the proposed rules were due Feb. 9, 2021.

Final rules and interpretive guidance: Broadly applicable

Holding Foreign Companies Accountable Act disclosure

On Dec. 2, 2021, the SEC approved new rules under the *Holding Foreign Companies Accountable Act*. Effective Jan. 10, 2022, the rule requires submission of certain documentation and certain disclosures when an entity files an annual report using an auditor that the PCAOB identifies as located in a jurisdiction not subject to its inspection.

Sample letter to China-based companies

In response to the increased risks of investing in China-based companies or companies that have the majority of their operations in China, Corp Fin staff published on Dec. 20, 2021, a sample letter to China-based companies that details the need for more prominent, specific, and tailored disclosure about these risks. The letter includes sample comments that Corp Fin may issue to China-based companies and highlights the need for detailed disclosures about the legal and operational risks associated with China-based companies and specific details regarding the structure of the entity. The letter also focuses on additional legal, regulatory, and enforcement risks that might exist.

Nasdaq board diversity rule

On Aug. 6, 2021, the SEC approved Nasdaq's new board diversity rule, which requires Nasdaq-listed entities to:

- Provide standardized annual public disclosure of board-level diversity statistics
- Maintain two directors, one female and the other of an under-represented minority or LGBTQ, or explain why it does not

The rule provides additional flexibility for smaller reporting companies, foreign issuers, and entities with five or fewer directors. It also specifies Nasdaq will provide one year of complimentary board recruiting services to eligible companies, which will facilitate identifying and evaluating diverse board candidates.

An entity must comply with the annual board-level diversity disclosure requirements by the later of Aug. 8, 2022, or the date the entity files its proxy or information statement for its annual shareholder meeting during 2022. The entity may provide the disclosure either in its SEC filings or on its website.

Entities must meet the requirement to have two diverse directors or explain why not, using a phased-in approach based on the Nasdaq tier on which the entity's securities trade. Nasdaq has provided a summary of the rule and transition requirements.

Proxy voting rules

Responding to Gensler's June 1, 2021, directive to SEC staff to consider whether to recommend further regulatory action specifically related to the September 2019 interpretation and guidance addressing the application of the proxy rules to proxy voting advice businesses and the July 2020 amendments to

Rules 14a-1(l), 14a-2(b), and 14a-9 concerning proxy voting advice, Corp Fin staff announced that it will not recommend enforcement action to the SEC based on the 2019 interpretation and guidance or the 2020 rule amendments during the period in which the SEC is considering further regulatory action in this area. Also, if regulatory action leaves the 2020 exemption conditions in place with the current compliance date of Dec. 1, 2021, the staff will not recommend any enforcement action based on those conditions for a reasonable period of time.

Guidance on conducting shareholder meetings

The SEC has updated sections of its staff guidance for conducting shareholder meetings in light of disruptions caused by the COVID-19 pandemic. The April 7, 2021, update addresses changes to the date, time, or location of a shareholder meeting and delays in printing and mailing of full sets of proxy materials. The April 9, 2021, update deals with presentation of shareholder proposals in person.

Updated guidance on confidential treatment orders

On March 9, 2021, Corp Fin updated its previously issued guidance in CF Disclosure Guidance Topic No. 7, "Confidential Treatment Applications Submitted Pursuant to Rules 406 and 24b-2." This guidance addresses how and what to submit when filing an application objecting to public release of information otherwise required to be filed under the *Securities Act* and the *Securities Exchange Act*.

Corp Fin updated the guidance on options for when a confidential treatment order is about to expire. Under the guidance, companies that previously have obtained a confidential treatment order have three choices of what to do when the order is about to expire. The options include refiling the unredacted information, extending the confidential period, and transitioning to compliance with the requirements under Regulation S-K Item 601(b)(10) and other parallel rules.

MD&A, selected financial data, and supplementary financial information

The SEC, on Nov. 19, 2020, adopted amendments that simplify and enhance certain Regulation S-K disclosure requirements. The amendments eliminate duplicative disclosures and modernize and improve management's discussion and analysis (MD&A) for the benefit of investors, while simplifying compliance efforts for registrants. Specifically, the requirement for selected financial data (Item 301) has been eliminated, the requirement to disclose supplementary financial information (Item 302) has been streamlined to replace the current requirement of quarterly tabular disclosure with a principles-based requirement for material retrospective changes, and MD&A (Item 303) requirements have been amended.

Among other changes to Item 303, changes to MD&A include clarifying disclosure requirements for liquidity and capital resources, streamlining disclosure requirement for results of operations, adding a new item for critical accounting estimates, replacing off balance sheet arrangements with a requirement to discuss such obligations in a broader context, eliminating tabular disclosure of contractual obligations, and streamlining required information regarding interim periods.

At the AICPA-CIMA conference, McCord, Corp Fin chief accountant, remarked that her office had received the most implementation questions about complying with the new disclosure guidance for liquidity and capital resources. She reminded audience members that the rule's adopting release stated the rule change was not intended to eliminate material information. She also remarked that the new rules included examples of the types of contractual requirements for cash that should be considered for disclosure and observed that the narrative discussion under the new rules might include periodic categories similar to those in the old contractual obligations table.

The rule was effective Feb. 10, 2021. Registrants are required to comply with the rule beginning with the first fiscal year ending on or after Aug. 9, 2021.

For filings after Feb. 10, 2021, registrants may choose to early adopt the final amendments as long as the amended item is adopted in its entirety. The final rule provides the following: "For example, upon effectiveness of the final amendments, a registrant may immediately cease providing disclosure pursuant to former Item 301, and may voluntarily provide disclosure pursuant to amended Item 303 before its mandatory compliance date. In this case, the registrant must provide disclosure pursuant to each provision of amended Item 303 in its entirety, and must begin providing such disclosure in any applicable filings going forward."

Acquisitions and dispositions of businesses and related pro forma information

On May 21, 2020, the SEC issued a final rule that revises the circumstances that require financial statements and related pro forma information for acquisitions and dispositions of businesses. The rule's intent is to allow for more meaningful conclusions about when an acquired or disposed business is significant as well as to improve the related disclosure requirements, including for real estate operations and investment companies.

The following table summarizes the most significant changes:

Topic	Final rule (new)	Current rule
Maximum number of required audited annual historical periods for financial statements of acquired businesses	Two	Three
Requirements for financial statements of acquired businesses in registration and proxy statements	Financial statements of an acquired business are not required in a registration or proxy statement, even if not previously filed or of major significance, once the acquisition has been consolidated for nine months or a full fiscal year, depending on significance.	Financial statements of an acquired businesses are required to be included in a registration or proxy statement when the financial statements have not been previously filed or are of major significance.
Income test*	Requires both a pretax income component and a revenue component to be met to trigger significance, using the lower of the two ratios to determine significance.	Includes a pretax income component only.
Investment test*	For acquisitions and dispositions of businesses only, allows comparison of investment in tested business to the issuer's average worldwide market capitalization over a specified period of time, when available.	Compares investment in subsidiary or business to issuer's total assets as of the prior fiscal year-end.
Pro forma information	Revises presentation of pro forma information and allows, in some cases, the option to present "management's adjustments" to show estimated and expected synergies and dis-synergies of the acquisition or disposition.	Expected synergies and dis-synergies do not typically meet criteria for pro forma adjustment and are not included in pro forma information.

*The final rule does not modify the current 20% significance threshold for the income, investment, or asset tests, which is the minimum level of significance that triggers a requirement to provide financial statements and related pro forma information of an acquired business. However, the final rule does increase the significance threshold triggering pro forma information for a business disposition from 10% to 20%.

The final rule also revises a number of other rules and forms, including expanding the use of pro forma information in significance tests, conforming significance tests for business dispositions and real estate acquisitions to those for business acquisitions, providing a specifically tailored significant subsidiary test for investment companies, and amending Form N-14 to address fund acquisitions by investment companies and business development companies.

The final rule was effective Jan. 1, 2021, for calendar year-end registrants and new registration statements; however, voluntary early compliance was permitted for registrants with a non-calendar year-end.

Coronavirus disclosure content guidance

On March 25, 2020, Corp Fin staff issued "Coronavirus (COVID-19): CF Disclosure Guidance: Topic No. 9," which summarizes the staff's views regarding disclosure and other securities law obligations that companies should consider with respect to COVID-19 impacts and disruptions.

On June 23, 2020, Corp Fin staff issued Disclosure Guidance Topic 9A, which is intended to supplement Disclosure Guidance Topic 9, issued March 25, 2020. Topic 9A provides the staff's views on three aspects of COVID-19-related disclosures. As noted in Topic 9A, disclosures should "enable an investor to understand how management and the Board of Directors are analyzing the current and expected impact of COVID-19 on the company's operations and financial condition, including liquidity and capital resources."

At the 2021 AICPA-CIMA conference, Corp Fin Chief Accountant McCord reminded participants that many of the principles and considerations in Disclosure Guidance Topic 9 and 9A remain relevant for year-end 2021 reporting.

Final rules and interpretive guidance: Industry focused

Comment letters in the banking industry

Under the *Sarbanes-Oxley Act of 2002*, the SEC's Division of Corporation Finance regularly reviews and occasionally comments on the filings of each SEC registrant. Crowe recaps recent themes from SEC comment letters for banking industry registrants to think about as they consider enhancements to their disclosures.

Statistical disclosures for banking registrants

On Sept. 11, 2020, the SEC adopted a final rule, "Update of Statistical Disclosures for Bank and Savings and Loan Registrants," to modernize statistical disclosures of banking registrants currently provided under Industry Guide 3, "Statistical Disclosure by Bank Holding Companies." The final rule clarifies the types of entities within its scope and carries over, updates, or eliminates various current Guide 3 disclosures. In addition, the rule rescinds Guide 3 and relocates required disclosures to new Subpart 1400 of Regulation S-K.

The rule clarifies, for both domestic and foreign registrants, that banks and savings and loan registrants are subject to Subpart 1400 and, with minor exceptions, matches the periods required for statistical disclosures to the annual and interim periods presented in the financial statements. The final rule carries over many current Guide 3 disclosures to Subpart 1400; however, it also eliminates certain Guide 3 disclosure topics (for example, return on equity and assets and short-term borrowings) and makes minor changes to Article 9 of Regulation S-X.

Among other changes, significant disclosure changes include weighted average yield of debt security investments by maturity, maturity analysis of the loan portfolio, certain credit ratios and the factors that explain material changes in the ratios, and the addition of certain disaggregated uninsured deposit disclosures.

The final rule was effective Nov. 16, 2020, and applies to years ended on or after Dec. 15, 2021. Voluntary early compliance was available provided the rules were adopted in their entirety.

Final rules and interpretive guidance: Market related

Shareholder proposal guidance

Corp Fin, on Nov. 3, 2021, issued Staff Legal Bulletin (SLB) No. 14L, "Shareholder Proposals," to provide information for companies and shareholders regarding Rule 14a of the *Securities Exchange Act of 1934*, which allows companies to exclude shareholder proposals from their proxy statements in certain circumstances.

Companies regularly request assurance that the SEC staff will not recommend enforcement action if they omit a proposal based on one of the exclusions ("no-action relief") set forth in Rule 14a-8. Accordingly, Corp Fin has issued this bulletin to streamline and simplify the process of reviewing no-action relief requests and to provide clarification of the standards applied to evaluate such requests. Upon issuance, this SLB replaces previously issued SLBs 14I, 14J, and 14K and provides guidance relating to proof of ownership letters and the use of graphics and images. The bulletin also provides new guidance on the use of email for submission of proposals, delivery of notice of defects, and responses to those notices.

This bulletin is not an SEC rule, regulation, or statement and does not alter or amend applicable law, and it creates no new or additional obligations.

In response the issuance of the bulletin, SEC Chair Gensler issued a statement, on Nov. 3, 2021, saying that the bulletin is consistent with the SEC's original intent under Rule 14a-8 and will provide greater clarity to companies and shareholders on understanding when exclusions may or may not apply.

Offering alternative views on the shareholder proposal guidance, Commissioners Peirce and Roisman also issued a statement on Nov. 3. 2021. Peirce and Roisman note that the new guidance fails to address the issues that the three rescinded bulletins were trying to resolve.

On Dec. 13, 2021, Corp Fin announced it would return to its historical practice of publicly posting all "no-action" letter responses. On Dec. 17, 2021, Corp Fin published an announcement providing guidance on personally identifiable and other sensitive information in Rule 14a-8 submissions and related materials. The guidance provides that effective immediately, companies and shareholder proponents should redact all personally identifiable and other sensitive information from Rule 14a-8 submissions and related materials prior to submitting them to the SEC.

New proxy rules

On Nov. 17, 2021, the SEC adopted final rules that require parties in a contested election to use universal proxy cards that include all director nominees presented for election at a shareholder meeting. The rule changes will allow shareholders to vote by proxy for their preferred combination of board candidates – similar to the rules for in-person voting. Additionally, to further facilitate shareholder voting in director elections, the SEC adopted amendments to make sure that proxy cards clearly specify the applicable shareholder voting options in all director elections and to require proxy statements to disclose the effect of a shareholder's election to withhold its vote. Compliance with the rules, which will be applicable to all nonexempt solicitations for contested elections other than those involving registered investment companies and business development companies, will be required for any shareholder meeting involving contested director election held after Aug. 31, 2022.

In response to the final rules, Commissioners Crenshaw, Lee, Roisman, and Peirce all issued statements.

Key market infrastructure for securities market data

The SEC adopted, on Dec. 9, 2020, a final rule modernizing the infrastructure for market data collection, consolidation, and dissemination for exchange-listed national market system (NMS) stocks. The changes reflect an "update and expand the content of NMS market data to better meet the diverse needs of investors in today's equity markets." The SEC has not extensively updated the rules addressing the content and dissemination of NMS market data since original implementation in the late 1970s. Under the rules, competitive forces are included in the national market system, which will increase the NMS market data and potentially benefit all market participants.

These rules are the latest initiative in the SEC's efforts to modernize the national market system to better fit the needs of investors and other market participants.

The rule was effective June 8, 2021.

Shareholder proposal rule

The SEC, on Sept. 23, 2020, adopted amendments to the shareholder proposal rule included in *Exchange Act* Rule 14a-8. The amendments seek to balance the interests of shareholders who submit proposals with the costs a company and other shareholders bear when the proposals are included in the company's proxy statement. The final rules apply to any proposal submitted for an annual or special meeting to be held on or after Jan. 1, 2022, and also provide for a transition period with respect to certain revised ownership thresholds for proposals submitted for an annual or special meeting to be held prior to Jan. 1, 2023.

Quotations for OTC securities

The SEC adopted, on Sept. 16, 2020, amendments to *Exchange Act* Rule 15c2-11. The amendments enhance disclosure and investor protection in the over-the-counter (OTC) market by requiring that broker-dealers do not publish quotations for an issuer's security when current issuer information is not publicly available, subject to certain exceptions.

The SEC says the amendments:

- Provide greater transparency to investors and other market participants by requiring that information about the issuer and its security be current and publicly available before a broker-dealer can begin quoting that security
- Limit broker-dealers' reliance on certain exceptions when issuer information is not available
- Provide exceptions to reduce unnecessary burdens on broker-dealers to quote certain OTC securities that may be less susceptible to fraud and manipulation

The final rule was effective Dec. 28, 2020, but it has a general compliance date nine months after the effective date and a compliance date two years after the effective date for certain financial information requirements.

Offerings

Securities offerings during extreme price volatility

While acknowledging the importance of capital formation, Corp Fin believes companies and investors should consider specific risks during periods of extreme market volatility and when a company's own securities exhibit extreme volatility. The impact of such risks can be more pronounced when a company seeks to raise capital during periods with:

- Significant stock price increases or recent divergences in valuation ratios
- High short interest or reported short squeezes
- Reports of strong and unusual retail investor interest

Such risks also might have a more significant impact on companies experiencing financial distress, liquidity challenges, or smaller public floats. Corp Fin believes that in these circumstances, explicit, tailored disclosures about market events and conditions, the company's situation, and the potential effect on investors are necessary to provide sufficient information for an investment decision.

To help address disclosures that might be necessary in such circumstances, Corp Fin released, on Feb. 8, 2021, an example letter containing comments that, depending on the particular facts and circumstances, Corp Fin may issue to companies that are seeking to raise capital in a volatile market. The sample comments in the letter do not represent a comprehensive list of the issues that companies should consider, and companies should appropriately tailor any disclosures to the entity's specific facts and circumstances. In addition, Corp Fin encourages companies to consider these comments in preparing disclosure documents that typically might not be subject to review by Corp Fin (for example,

automatically effective registration statements or prospectus supplements for shelf takedowns from an already effective registration statement). Corp Fin indicates any company with questions on proposed disclosures should consider contacting the industry office responsible for the company's filings.

Exempt offering framework improvements

The SEC voted, on Nov. 2, 2020, to amend its rules to address gaps and complexities in the exempt offering framework. The amendments are designed to promote capital formation and expand investment opportunities while preserving or improving investor protections as well as increasing access to capital for issuers.

In general, the amendments:

- Establish – in one broadly applicable rule – the ability of issuers to move from one exemption to another
- Expand the offering limits for Regulation A, Regulation Crowdfunding, and Rule 504 offerings, and adjust certain individual investment limits
- Provide specific rules governing certain offering communications, including permitting some "test-the-waters" and "demo day" activities
- Standardize certain disclosure and eligibility requirements and bad actor disqualification provisions

The final rules were effective March 15, 2021, except for certain rules and the amendments to the introductory paragraph in the "Optional Question and Answer Format for an Offering Statement" section of Form C, which are effective from Jan. 14, 2021, until March 1, 2023.

Financial disclosure requirements for registered debt offerings

The SEC adopted, on March 2, 2020, amendments to the financial disclosure requirements for registered debt offerings that include credit enhancements, such as subsidiary guarantees, or affiliates whose securities are pledged as collateral. The requirement changes are designed to improve the quality of disclosure and increase the likelihood that issuers will complete registered debt offerings.

Included among the disclosure requirement changes, the SEC reduced the circumstances that require separate audited financial statements of subsidiary issuers and guarantors. In place of requiring separate statements, the SEC simplified the required alternative disclosures. Regarding separate financial statements of affiliates whose securities are pledged as collateral for registered securities, the SEC revised the required disclosure to be similar to those for subsidiary issuers and guarantors.

The final rule was effective Jan. 4, 2021; however, early voluntary compliance was permitted.

Special purpose acquisition companies

Chair remarks on SPACs

Chair Gensler presented prepared remarks before the Small Business Capital Formation Advisory Committee on Sept. 27, 2021. Gensler concentrated his remarks on the unprecedented surge in SPACs, which provide an alternative to traditional IPOs. He said the many costs of SPACs include sponsor fees, dilution for the private investment in public equity investors, and fees for investment banks and financial advisers. He has requested recommendations from the SEC staff about how the SEC might update its rules so that investors are better informed about the fees, costs, and conflicts that might exist with SPACs. He said that enhanced disclosures and other provisions can increase competition in this market and shared a final thought that "it is worth considering what we have learned from SPACs and direct listings, and whether there are any changes that might be appropriate for traditional IPOs."

At the Healthy Markets Association Conference on Dec. 9, 2021, Gensler delivered a speech expressing his thoughts on the use of SPACs to go public. Gensler said that SPACs have many moving parts and a two-step structure that creates additional conflicts. He identified that conflicts exist between investors that remain throughout the deal and those that cash out after voting. Gensler has requested from the SEC staff proposals "around how to better align the legal treatment of SPACs and their participants with the investor protections provided in other IPOs, with respect to disclosure, marketing practices, and gatekeeper obligations."

Additionally, Gensler has asked the SEC to provide recommendations about how investors might be better informed about the fees, projections, dilution, and conflicts that may exist during all stages of SPACs and how investors can receive those disclosures at the time they're deciding whether to invest. As part of this process, the SEC staff also is considering clarifying disclosure obligations under existing rules.

Gensler also discussed concerns about who is performing the role of "gatekeepers" in the SPAC transaction process. He said that the gatekeepers may include directors, officers, SPAC sponsors, financial advisers, and accountants. Gensler said that there may be "some who attempt to use SPACs as a way to arbitrage liability regimes. Many gatekeepers carry out functionally the same role as they would in a traditional IPO but may not be performing the due diligence that we've come to expect." With regard to liability, he warned that "SPACs do not provide a 'free pass' for gatekeepers." Recommendations are expected from the SEC staff about how the SEC can better align incentives between gatekeepers and investors as well as how the SEC can address the status of gatekeepers' liability obligations. With a word of caution, Gensler reminded the audience that as these recommendations are being developed, the SEC's Division of Enforcement will continue to make sure that investors are being protected in the SPAC area.

Statement on SPACs

On April 8, 2021, acting Corp Fin Director Coates released a statement discussing SPACs, IPOs, and liability risk under the securities laws. He says that over the past six months, a significant increase in the use and popularity of SPACs has raised concerns and has increased the scrutiny over these transactions as they continue to evolve.

Coates shares that SEC staff members are continuing to look carefully at SPAC filings and disclosures and their private targets and are providing guidance so that the public can make informed investment and voting decisions about these transactions. The statement also describes basics of a typical SPAC and notes some of the complexities of the transactions. SPACs might offer private companies an alternative pathway to go public and obtain a stock exchange listing, a broader shareholder base, status as a public company with *Exchange Act* registered securities, and a liquid market for its shares, and this raises questions regarding securities law liability exposure, investor protections, and other filing requirements.

In his statement, Coates says that all those involved in promoting, advising, processing, and investing in SPACs should understand the limits on any alleged liability difference between SPACs and conventional IPOs. He adds that providing greater clarity on the scope of the safe harbor in the *Private Securities Litigation Reform Act* might offer advantages.

Coates' statement follows the release of a March 31, 2021, staff statement on SPACs. That statement addresses certain accounting, financial reporting, and governance issues that should be carefully considered before a private operating company undertakes a business combination with a SPAC.

On March 31, 2021, acting Chief Accountant Munter also issued a statement, which outlines considerations relating to markets and timing, financial reporting, internal controls, corporate governance, and audit committees. Munter's statement provides auditing considerations, including independence issues relating to de-SPAC mergers (that is, the combination of the SPAC with the target operating company).

On April 12, 2021, Coates and Munter issued a statement on accounting and reporting considerations for warrants issued by SPACs. The statement provides that certain warrants issued by a SPAC should be classified as liabilities rather than equity and, therefore, these warrants would need to be measured at fair value, with the changes in fair value included in net income. As this treatment may require some SPACs to change their classification of certain warrants, companies and their auditors should consider whether financial statements previously filed contain a material error that would require restatement.

Technology and innovation

Chair and commissioners on crypto markets

On, Dec. 2, 2021, SEC Chair Gensler and Commissioner Peirce delivered remarks before the Investor Advisory Committee on crypto markets and regulatory concerns.

Gensler shared thoughts on the crypto markets, including:

- The markets have been catalysts for change and innovation.
- As this asset class has $2.6 trillion aggregate market capitalization, it belongs inside public policy.
- The asset class is full of fraud, scams, and abuse.
- The crypto market does not have sufficient investor protection, and existing protections have significant gaps.

He noted that these items leave the crypto markets open to manipulation and investors vulnerable. He warned that it is best to be preemptive in addressing investor protection issues and not wait until a major issue arises. Further, he cautioned that "financial innovations throughout history don't long thrive outside of our public policy frameworks."

In her remarks, Peirce also reiterated the importance of investor protections in the crypto markets and specifically touched on other areas of investor protection that are important to consider, including:

- **Regulatory clarity.** Peirce said that the SEC has not provided clarity in response to repeated questions, which has led to enforcement actions. She requested the committee urge the SEC to address the tough questions surrounding the crypto markets' identification, trading, platforms, and custody.
- **Investor access.** She noted that while the SEC recently started permitting bitcoin futures-based exchange-traded funds, the commission has yet to approve a spot exchange-traded product.
- **Individual liberty.** She wondered if the SEC could regulate with a "lighter hand" so as to not use regulation to force investors into the SEC's "comfort zone."

In addition to the remarks made by Gensler and Peirce, the International Journal of Blockchain Law published a statement by Commissioner Crenshaw on Nov. 9, 2021. It includes a discussion of the advantages and shortfalls of decentralized finance (DeFi). She says that DeFi presents a multitude of opportunities; however, it also poses important risks and challenges for regulators, investors, and the financial markets. She includes background on the current regulatory landscape for DeFi, the SEC's role, and two structural hurdles that should be addressed. The hurdles that Crenshaw identifies are pseudonymity and lack of transparency, both of which make it easier to conceal manipulation.

President's Working Group report on stablecoin regulations

In a report released on Nov. 1, 2021, the President's Working Group on Financial Markets, working in conjunction with the Federal Deposit Insurance Corp. and the Office of the Comptroller of the Currency, examines potential risks and regulatory gaps related to stablecoins (cryptocurrencies that are valued by a specified reserve asset) and offers recommendations for mitigating these risks. The report outlines some background on the growing use of stablecoins in the U.S. digital asset markets and describes a range of risks associated with increased stablecoin-related activities including risk of fraud, misappropriation, conflict of interest, market manipulation, money laundering, and terrorist financing, among others.

In response, SEC Chair Gensler issued, on Nov. 1, 2021, a statement describing the report as thoughtful. He said the use of stablecoins presents many public policy challenges, and the SEC and the Commodity Futures Trading Commission (CFTC) will deploy, as applicable, the full protections of the federal securities laws and the *Commodity Exchange Act* to stablecoin arrangements.

Request for comments on broker-dealer and investment adviser digital practices

The SEC, on Aug. 27, 2021, issued a request for information and public comment on broker-dealers' and investment advisers' use of digital engagement practices. These digital engagement practices include behavioral prompts, differential marketing, game-like features, other design elements or features aimed at engaging with retail investors on digital platforms, and the analytical and technological tools and methods used. Investment advisers use these tools to develop and provide investment advice and use analytical tools to learn more about their clients to develop investment advice based on that information.

The SEC is issuing the request primarily to:

- Develop a better understanding of the market practices associated with the use of digital engagement practices and the related analytical and technological tools and methods
- Learn what conflicts of interest may arise from optimization practices and whether those practices affect the determination of whether digital engagement practices are making a recommendation or providing investment advice
- Provide market participants and other interested parties an avenue to share their perspectives on the use of digital engagement practices and the related tools and methods
- Facilitate the SEC's assessment of existing regulations and consideration of whether regulatory action may be needed including additional investor protections

Comments on the request were due Oct. 1, 2021.

Remarks on digital engagement practices, crypto assets, and disclosures

On Sept. 1, 2021, Chair Gensler provided remarks on digital engagement practices, crypto assets, and disclosures before the European Parliament Committee on Economic and Monetary Affairs.

Considering the evolving area of technology and finance, Gensler discussed the use of predictive data analytics underlying the trading and wealth management apps flooding the market that use individualized marketing and behavioral prompts that encourage users to engage more with a digital platform. These tools are designed to increase platform revenues, data collection, and customer engagement, leading to potential conflicts between the platform and investors. The use of these digital enhancement practices raises questions as to how investors are protected, what the implications are under the securities laws, and how these tools and models ensure fairness of access and pricing. He highlighted the SEC's request for information and comment on digital engagement practices issued on Aug. 27. He warned of his concern that the broad adoption of deep learning models could contribute to a future crisis.

In his remarks about crypto assets, Gensler reiterated his position that the SEC needs to ensure it is achieving its public policy goals and protecting investors and consumers, guarding against illicit activity, and ensuring financial stability. He noted that most crypto platforms provide direct access for investors with no broker between the public and the platform, which creates vulnerability as no clear investor protection obligations exist on these platforms. Gensler added that the use of stablecoins on these platforms may aid those looking to avoid many of the public policies existing in the traditional banking and financial system such as anti-money laundering policies.

Lastly, recognizing investors' increased demand for additional disclosures to understand climate risks, workforces, and cybersecurity risks of the companies they invest in, Gensler shared that he asked the SEC staff to develop a proposal for climate risk disclosure requirements and to examine information that can be learned from other frameworks and standards. He said he directed staff to review current fund branding practices and make recommendations about whether fund managers should disclose the criteria and underlying data they use to market themselves, and to consider disclosure requirements about human capital and board diversity.

Remarks on investor protections for crypto assets

On Aug. 3, 2021, before the Aspen Security Forum, SEC Chair Gensler discussed the current environment for crypto asset investing and trading and identified the need for greater investor protections. Gensler said that the crypto asset class is currently worth approximately $1.6 trillion without enough investor protections over crypto assets. He warned about scams and frauds across the asset class and said no structure is in place to provide comprehensive information to investors as these assets often trade and move outside of established regulatory frameworks, platforms, and regulations.

Gensler said that trading platforms where crypto assets are being bought, sold, and traded might include unregistered securities. Therefore, these are not being regulated as other registered securities are, and they are missing required disclosures and market oversight. This creates significant gaps in investor protections. Further, Gensler said he believes these trading platforms are potentially skirting securities, commodities, and banking laws. He also touched on custody of crypto assets and noted that custody protections are important to preventing theft and protecting investors.

To address the regulatory gaps, Gensler called on Congress to act on crypto asset legislation. He noted that the SEC is ready to work with Congress, the administration, and other regulators and partners to address regulatory gaps and focus on trading and lending platforms.

Lack of guidance on digital asset trading

On July 14, 2021, SEC Commissioners Peirce and Roisman released a public statement addressing the lack of clarity for market participants around the application of the securities laws to digital assets and their trading. Referring to the recent Coinschedule Ltd. SEC order, which found that a publicized token offering included investment contracts, which are securities and therefore subject to securities laws, the commissioners expressed their disappointment that the order did not explain which digital assets in the offering were securities or how that was determined, which would have provided additional guidance.

Peirce and Roisman noted that although the SEC has provided some guidance and people can use and analogize settled SEC enforcement actions to determine if the tokens are securities, not enough clear guidance exists for the large number of factors to consider. Clues can be gathered from enforcement actions to make determinations; however, applying those clues to the facts of a completely different token offering does not necessarily produce clear answers. Peirce and Roisman both concluded that the SEC needs to prepare better guidance with clear and timely answers, as providing guidance piecemeal through enforcement actions is not the best way to move forward in this complex and evolving marketplace.

Statement on digital asset securities custody by broker-dealers

The SEC issued, on Dec. 23, 2020, a statement and request for comment regarding the custody of digital asset securities by broker-dealers. The statement addresses the application of the *Securities Exchange Act* Rule 15c3-3 to digital asset securities.

The SEC press release about the statement details the SEC's position as follows: "For a period of five years, a broker-dealer operating under the circumstances set forth in the statement will not be subject to a Commission enforcement action on the basis that the broker-dealer deems itself to have obtained and maintained physical possession or control of customer fully paid and excess margin digital asset securities for the purposes of paragraph (b)(1) of Rule 15c3-3. These circumstances, among other things, include that the broker-dealer limits its business to digital asset securities, establishes and implements policies and procedures reasonably designed to mitigate the risks associated with conducting a business in digital asset securities, and provides customers with certain disclosures regarding the risks of engaging in transactions involving digital asset securities."

As part of the statement, the SEC requested comments to specific questions to gather additional insight into the developing standards and best practices for custody of digital asset securities. The information gathered as part of this request will serve to inform potential future SEC actions.

The statement and request for comment were effective April 27, 2021.

Cybersecurity: Sanctions charging deficient cybersecurity procedures

On Aug. 30, 2021, the SEC announced the sanctioning of eight firms in three actions for failures in their cybersecurity policies and procedures that resulted in cloud-based email account takeovers exposing personally identifying information of thousands of customers and clients at each firm. The firms were SEC-registered broker-dealers, investment advisory firms, or both. Specifically, the SEC noted that accounts taken over were not protected consistent with firm policies, breach notifications to the firms' clients included misleading language, and some of the firms failed to timely adopt and implement firmwide enhanced security policies and procedures after initial discovery of email account takeovers.

The SEC's orders against each of the firms found that the firms violated Rule 30(a) of Regulation S-P, known as the Safeguards Rule. The Safeguards Rule is aimed at protecting confidential customer information. For two of the firms, the orders also found that the entities violated Section 206(4) of the *Advisers Act* and Rule 206(4)-7 in connection with their breach notifications to clients. Without admitting or denying the SEC's findings, each firm agreed to cease and desist from future violations of the charged provisions, to be censured, and to pay a penalty.

Leadership changes

SEC commissioner resignation

On Dec. 20, 2021, Commissioner Roisman announced his intention to resign his position as commissioner by the end of January 2022.

New SEC general counsel

On Sept. 28, 2021, the SEC announced that Dan Berkovitz, a CFTC commissioner, was named SEC general counsel, effective Nov. 1, 2021. Berkovitz replaced John Coates, who will return to teaching at Harvard University. Berkovitz has served as a CFTC commissioner since September 2018. Prior to that he was a partner and co-chair of the futures and derivatives practice at the law firm WilmerHale, an adjunct professor at Georgetown University Law School, and vice chair of the American Bar Association Committee on Derivatives and Futures Law. He also served as the CFTC's general counsel from 2009 to 2013.

SEC senior adviser to the chair

The SEC announced, on Aug. 25, 2021, the appointment of Barbara Roper as senior adviser to Chair Gensler. Roper's focus will be on issues and policies relating to retail investor protections, broker-dealer and investment adviser oversight, and examinations. She joins the SEC from her role as Director of Investor Protection for the Consumer Federation of America. Roper worked at the Consumer Federation of America for 35 years and has been a leading consumer spokesperson on investor protection issues, specifically the standards that apply to investment professionals that investors rely on for advice and recommendations, and she plans to bring that same focus to the SEC.

New SEC enforcement director

On June 29, 2021, the SEC announced that Gurbir S. Grewal was named director of the Division of Enforcement, effective July 26, 2021. Prior to that, Grewal served as the New Jersey attorney general beginning in January 2018.

New SEC Corp Fin director and chief counsel

On June 14, 2021, the SEC announced that Renee Jones was appointed director of Corp Fin. John Coates, Corp Fin's acting director, was named SEC general counsel. Both appointments were effective June 21, 2021. Jones most recently taught courses on various aspects of corporate and securities law and governance while serving as professor of law and associate dean for academic affairs at Boston College Law School. Previously, she practiced at Hill & Barlow law firm.

Coates served as Corp Fin's acting director since February 2021.

New SEC DERA chief economist and director

The SEC announced, on May 3, 2021, that Jessica Wachter was named chief economist and director of the Division of Economic and Risk Analysis (DERA). She had been a professor at the Wharton School at the University of Pennsylvania since 2003 and is a leading academic researcher on financial markets. DERA is involved in a wide range of SEC activities, including policymaking, rulemaking, enforcement, and examination, and the division assists in identifying, analyzing, and responding to economic and market issues. DERA also provides subject-matter expertise and cost-benefit economic analysis for rule proposals and final rules.

SEC chair swearing in

On March 2, 2021, Gary Gensler, President Joe Biden's nominee for the position of SEC chair, appeared before the Senate banking committee. On March 10, 2021, the committee voted 14-10 to approve Gensler both for the remainder of the term of retired Chair Clayton ending on June 5, 2021, and for a full term ending on June 5, 2026. The Senate confirmed Gensler as SEC chair on April 14, 2021, and he was sworn in on April 17.

Senior policy adviser for climate and ESG

On Feb. 1, 2021, the SEC announced that Satyam Khanna will serve as senior policy adviser for climate and ESG issues to acting Chair Lee and said Khanna will guide SEC initiatives on climate risk and ESG developments. Most recently, Khanna was a resident fellow at New York University School of Law's Institute for Corporate Governance and Finance, and he served on the Biden-Harris presidential transition team for financial regulation.

Departure of SEC chief accountant; new acting chief accountant

On Jan. 13, 2021, the SEC announced Sagar Teotia, chief accountant, would conclude his tenure in February. The SEC announced, on Jan. 22, 2021, that Paul Munter would be acting chief accountant upon Teotia's departure in February 2021. Since 2019, Munter had served as deputy chief accountant, where he led the Office of the Chief Accountant's international work. As acting chief accountant, Munter serves as the primary adviser to the SEC on accounting and auditing matters and is responsible for assisting the SEC in its oversight of the FASB and the PCAOB. Munter has a Ph.D. in accounting from the University of Colorado and has served as a deputy chief accountant leading OCA's international work since 2019.

From the Office of Compliance Inspections and Examinations

2021 examination priorities

On March 3, 2021, the SEC's Division of Examinations announced its 2021 examination priorities. Per the announcement, the 2021 examinations will include a greater focus on climate and ESG-related risks and will also focus on, among other topics, these areas:

- Compliance with Regulation Best Interest, Form CRS, and whether registered investment advisers have fulfilled their fiduciary duties of care and loyalty
- Information security and operational resiliency, including review of entities' business continuity and disaster recovery plans to confirm that they are accounting for the increasing physical and other relevant climate change and related risks
- Financial technology and innovation, including digital assets
- Compliance with anti-money laundering requirements
- LIBOR transition
- Investment advisers and investment companies, including compliance programs, registered funds, and registered investment advisers to private funds
- Broker-dealers and municipal advisers, including compliance with the Customer Protection Rule and the Net Capital Rule; the adequacy of internal processes, procedures, controls, and compliance with requirements; and whether municipal advisers have met their fiduciary duty obligations to municipal entity clients
- Market infrastructure including clearing agencies, national securities exchanges, regulation systems compliance and integrity, and transfer agents

The listing of 2021 priorities is not meant to be comprehensive and will not be the only areas the SEC will focus on in its examinations, risk alerts, and outreach.

From the Division of Enforcement

Enforcement director and chief accountant remarks

On Dec. 9, 2021, at the AICPA-CIMA conference, the director, Gurbir Grewal, and chief accountant, Matthew Jacques, of the SEC's Division of Enforcement observed that trust in the capital markets rests on three pillars of robust:

- Enforcement
- Remedies
- Compliance

If all three pillars are solid, then the financial reporting ecosystem will build and enhance trust. Grewal remarked that the first two pillars rest on regulators, and his intent is to quickly bring enforcement actions with specific, tailored remedies designed as deterrents. Compliance falls to gatekeepers, and Grewal and Jacques encouraged gatekeepers to hold companies accountable and not succumb to undue pressures.

Grewal provided three example cases the staff had brought during 2021 and remarked on three takeaways:

- Transparency disclosure of how an entity reached numbers is as important as the accuracy of those numbers.
- Effective internal accounting controls are critical to companies and investors alike.
- Accounting is not an "aspirational" reporting model. Companies should take care to report what actually happened and not what the company hopes happened.

Jacques reminded participants that the pandemic continues to affect financial reporting and challenged all stakeholders to evaluate the current state of their internal controls. He also provided reminders of the importance of materiality in the evaluation of both accounting errors and the effectiveness of internal control over financial reporting.

From the Public Company Accounting Oversight Board (PCAOB)

PCAOB annual report and strategic plan

PCAOB 2020 annual report

The PCAOB published its "2020 Annual Report" in May 2021. The report summarizes the PCAOB's operations and financial results for fiscal year 2020 and highlights accomplishments and developments for the year for each of the PCAOB's five strategic goals, which are described in the strategic plan. Additionally, the report includes audited financial statements, a financial review, and management's report on internal control over financial reporting.

PCAOB 2022 budget and five-year strategic plan

On Nov. 23, 2021, the PCAOB approved its fiscal year 2022 budget, which the SEC subsequently approved on Dec. 15, 2021, based on its five-year strategic plan for 2020 through 2024, which guides the PCAOB's programs, operations, and budget.

The plan includes the following goals:

- "Drive improvement in the quality of audit services through a combination of prevention, detection, deterrence, and remediation."
- "Anticipate and respond to the changing environment, including emerging technologies and related risks and opportunities."
- "Enhance transparency and accessibility through proactive stakeholder engagement."
- "Pursue operational excellence through efficient and effective use of our resources, information, and technology."
- "Develop, empower, and reward our people to achieve our shared goals."

PCAOB leadership changes and priorities

New PCAOB chair and board members

The SEC, on Nov. 8, 2021, announced the appointments of Erica Y. Williams as the new chair of the PCAOB and Christina Ho, Kara M. Stein, and Anthony C. Thompson as new board members. Duane DesParte, current acting chair, will continue to serve in that role until Williams is sworn in. On Nov. 9, 2021, the PCAOB announced that Ho was sworn in as a board member. Her term will run through Oct. 24, 2025. On Nov. 18, 2021, the PCAOB swore in Stein as a board member. Her term will run through Oct. 24, 2026. On Jan. 3, 2022, Thompson, whose term will run through Oct. 24, 2022, was sworn in as a PCAOB board member. Williams was sworn in on Jan. 10, 2022, and will serve until Oct. 24, 2024.

Research and standard-setting

Acting chief auditor speech at AICPA-CIMA conference

On Dec. 7, 2021, PCAOB acting chief auditor Barbara Vanich remarked on the PCAOB's current standard-setting agenda, which includes projects on quality control and using other auditors. Vanich also made observations about the PCAOB's research agenda including data and technology and audit evidence.

New standards advisory group

At its meeting on March 29, 2021, the PCAOB unanimously approved the formation of a new standards advisory group (SAG) that will increase stakeholder engagement and provide opportunities for investors and other stakeholders to advise the PCAOB on key initiatives.

As detailed in its charter, the purpose of the SAG is to advise the PCAOB on:

- Existing auditing and related attestation standards as well as quality control, ethics, and independence standards
- Proposed standards
- Potential new or amended standards
- Matters other than standards that are significant to the PCAOB

The SAG will perform specific tasks assigned by the PCAOB, and task forces of the SAG will play a critical role in deliberating, producing deliverables, and sharing information on key issues. The charter establishes an 18-person group of experts, with representatives from the investor community (five), external auditors (four), audit committee members or directors (three), financial reporting oversight personnel (three), and academics and others with specialized knowledge (three).

On April 12, 2021, the PCAOB announced that it is seeking nominations for the SAG for both the 2021-2023 term and the 2021-2024 term. Nominees must meet certain qualifications described in the SAG charter. Links to nomination forms are in the announcement.

Subsequently, on June 22, 2021, the acting PCAOB chair announced a pause in the search for new members as the PCAOB intends to reassess its stakeholder engagement and advisory groups.

Research projects on the agenda

The PCAOB's research agenda includes two projects of note – one on audit evidence and one on data and technology. For the audit evidence project, the staff is assessing whether a need exists for guidance or changes to Auditing Standard (AS) 1105, "Audit Evidence," considering the increasing use of technology-based tools and the increasing availability and use of information from sources external to the company, both in the financial reporting process and as audit evidence.

The research project on data and technology focuses on determining whether a need exists for guidance, changes to PCAOB standards, or other regulatory actions considering the increased use of technology-based tools by auditors and preparers. Advancements in technology affect the nature, timing, preparation, and use of financial information, and auditors are expanding their use of technology-based tools, including data analytics, to plan and perform audits. Innovations in such technologies have the potential to improve the efficiency and effectiveness of both the audit and the financial reporting process.

Quality control

On Dec. 17, 2019, the PCAOB issued a concept release, "Potential Approach to Revisions to PCAOB Quality Control Standards," covering potential updates to the PCAOB's quality control (QC) standards. The AICPA developed the current QC standards applicable to PCAOB audits. However, those standards existed prior to the PCAOB, and the auditing environment has changed significantly since that time. Allowing for efficiencies for firms complying with both PCAOB and international standards, the concept release is based in part on proposed international quality control standards with certain incremental or alternative requirements specific to auditing under PCAOB standards (for example, U.S. federal securities laws, SEC rules and regulations, specific PCAOB observations). In conjunction with the issuance of the concept release, PCAOB Chairman William Duhnke noted, "[a]n effective quality control system within an audit firm can serve to prevent, identify, and remediate audit quality deficiencies…[t]he input we receive from the public through this concept release will play an important role in the Board's consideration of an approach to revising our quality control standards."

Comments were due March 16, 2020.

PCAOB coronavirus response

COVID-19 spotlight document

The PCAOB, on Dec. 2, 2020, posted "Staff Observations and Reminders During the COVID-19 Pandemic." This report offers lessons learned from recent PCAOB inspections of reviews of interim financial information and audits, and it provides important reminders for auditors to consider as they plan for and perform audits in the current pandemic environment. The reminders and key takeaways section includes insights into concerns over internal control over financial reporting, significant judgments and accounting estimates, and a reminder regarding the need for consideration of COVID-19 disclosures and risks.

Inspections and enforcement

Final inspection and investigations rule

On Sept. 22, 2021, the PCAOB adopted a final rule related to its responsibilities under the *Holding Foreign Companies Accountable Act* (HFCAA). The HFCAA requires the board to determine and communicate to the SEC whether it is unable to inspect or investigate registered public accounting firms located in a foreign jurisdiction. The SEC, in certain circumstances under the law, will be required to take further action related to registrants with audit opinions rendered in those foreign jurisdictions. The final rule was approved by the SEC on Nov. 4, 2021.

Preview of 2020 inspection observations

The PCAOB issued, on Oct. 18, 2021, a publication, "Spotlight: Staff Update and Preview of 2020 Inspection Observations," that provides observations from the 2020 inspections of audits of issuers prior to issuance of the inspection reports, which audit committees might find useful when engaging with their auditors. The report highlights changes in the PCAOB inspection approach, common deficiencies, observations related to quality control, observations on good practices, and responses to technology developments including cybersecurity, distributed ledger technologies, and digital assets. While recurring deficiencies are similar to those in prior years, the PCAOB did observe improvements in auditing accounting estimates. The publication notes, however, that deficiencies continue to occur, particularly in auditing the allowance for loan losses.

Staff observations at the AICPA-CIMA conference

George Botic, director of the Division of Inspections, and Patrick Bryan, director of the Division of Enforcement, provided further perspectives at the AICPA-CIMA conference. Botic addressed five topics including:

- Changes made in 2021 inspections
- Recurring deficiencies (for example, business combinations, inventory, revenue, ICFR, allowance for loan and lease losses)
- Importance of firms' QC systems
- Forecast of 2022 focus areas (for example, impact of the current economic environment, mergers and acquisitions, supply chain disruptions, pandemic impacts, SPACs, independence due to nonaudit services, carrying broker dealers)
- Key takeaways for participants:
    - Continued importance of exercising due professional care and professional skepticism throughout the audit
    - Performance of thorough and continuous risk assessment – the need for practitioners to understand the impact of known and potential changes due to current economic climate and perform procedures to address the risk
    - Fraud procedures and the importance of incorporating unpredictability

Bryan discussed the Enforcement Division's 2021 focus areas, significant enforcement cases, and his perspective on the enforcement outlook for 2022.

Annual broker-dealer inspection report

On Aug. 19, 2021, the PCAOB released its annual report on the 2020 interim inspections of broker-dealer auditors. The report includes observations from inspections during 2020, guidance and examples of effective procedures, and information about the inspection approach. The report highlights that the percentage of deficiencies for audit and attestation engagements dropped 14% from 2019 – however remained high – and that continued improvement is needed.

With the annual inspection report, the PCAOB released, "Supplementary Information Related to Audits of Brokers and Dealers," which provides comparative data about selected firms and engagements and the results of PCAOB inspections over multiyear periods.

The PCAOB also noted this report should help broker-dealer owners and audit committees or equivalents as they oversee the work of their auditors and engage on financial reporting.

Staff outlook and audit committee resources on 2021 inspections

On April 6, 2021, the PCAOB issued two documents to help auditors and audit committees understand the PCAOB's 2021 inspection focus:

- "Spotlight: Staff Outlook for 2021 Inspections" provides information auditors might find useful as they plan and perform current and upcoming audits. The document addresses the principal changes the PCAOB plans for 2021 inspections and other areas of planned inspection focus:
    - Audit areas with continued deficiencies
    - Firms' quality control systems
    - How firms comply with auditor independence requirements
    - Fraud procedures
    - Critical audit matters
    - How firms implement new auditing standards
    - Supervision of audits involving other auditors
    - Responding to cyberthreats
    - Auditing digital assets
- Audit committees can use the "Staff Outlook for 2021 Inspections" document with the companion "Audit Committee Resource: 2021 Inspections Outlook" to engage in meaningful dialogue with their auditor on topics including the auditor's risk assessment, firms' quality control systems, how firms comply with auditor independence, fraud procedures, critical audit matters, how firms implement new auditing standards, and supervision of audits involving other auditors.

Other matters of interest

Audit committee insights

As part of the PCAOB's strategic goal of enhancing transparency and accessibility through proactive stakeholder engagement, the PCAOB released, on Feb. 1, 2021, "2020 Conversations With Audit Committee Chairs," which summarizes feedback received from outreach conducted during 2020. This report provides a summary of perspectives from approximately 300 audit committee chairs at U.S. public companies whose audits the PCAOB inspected. The report focuses on three topics: the auditor and communications with the audit committee, new auditing and accounting standards, and emerging technologies. For each topic area, the PCAOB has provided a list of what is working well as identified by the audit committee chairs.

On July 31, 2020, the PCAOB posted "Conversations With Audit Committee Chairs: COVID-19 and the Audit," which summarizes the results of discussions with audit committee chairs on their thoughts about COVID-19's effects on financial reporting and the audit. Audit committee chairs said they are focusing on numerous topics that present increased financial reporting and audit risk. The two main areas

highlighted in the report are increased risks associated with remote work and increased communications with auditors. The document identifies forms of communication that audit committee chairs found helpful and provides suggestions for communication with the auditors during the pandemic. It also includes example questions to discuss with auditors regarding the additional risks remote work might present related to productivity, timing, testing, technology matters, and cybersecurity concerns.

Forum on auditing small businesses and broker-dealers

On Sept. 20, 2021, the PCAOB announced that the 2021 forum for auditors of small businesses and auditors of broker-dealers will be prerecorded and made available on its website starting Oct. 20, 2021. The recordings include perspectives from the PCAOB and the Financial Industry Regulatory Authority.

Auditor independence

On Nov. 19, 2020, the PCAOB adopted amendments to the PCAOB interim independence standards and PCAOB rules to align with the changes that the SEC recently made to its auditor independence rules. The proposed amendments were published in the Federal Register on Nov. 27, 2020, for public comment. Comments were due Dec. 18, 2020.

The SEC issued an order on Jan. 14, 2021, to approve the amendments. The rules were effective June 9, 2021.

From the American Institute of Certified Public Accountants (AICPA)

ESG-related matters practice aid

On Dec. 5, 2021, the AICPA and CIMA released a new practice aid titled "Considerations of ESG-Related Matters in an Audit of Financial Statements." The practice aid addresses the responsibilities of management, those charged with governance, and the auditor when considering climate-related matters in an audit of financial statements.

Credit losses A&A guide

On Nov. 11, 2021, the AICPA issued its long-awaited credit losses audit and accounting (A&A) guide. In addition to addressing items covered in the September 2019 practice aid, the guide provides implementation observations and adds a new chapter for accounting issues addressed by the FASB's Credit Losses Transition Resource Group or the AICPA's Financial Reporting Executive Committee (FinREC) as follows:

- Scope exception for loans and receivables between entities under common control
- Scope of purchased financial assets with credit deterioration guidance for beneficial interests within FASB ASC 325-40
- Application of FASB ASC 325-40 for trading securities
- Refinancing and loan prepayments
- Measurement inputs for short-term arrangements
- Discounting inputs using a method other than a discounted cash flow method
- Reasonable and supportable forecast – developing the period and use of historical information
- Reversion method: estimation versus accounting policy
- Determining the life of a credit card receivable
- Zero expected credit losses
- Accounting for TDRs
- Capitalized interest
- Gains and losses on subsequent disposition of leased assets
- Accounting for changes in foreign exchange rates
- Inclusion of future advances of taxes and insurance payments
- Considerations related to FASB ASC 326 for insurance-entity-specific balances
- Transition guidance for pools of financial assets
- Application of subsequent events

CECL implementation guidance for broker-dealers

The brokers and dealers in securities A&A guide has been updated to incorporate guidance addressing implementation of ASC Topic 326.

The updates include the following:

- A new section in Exhibit 6-8, Note 2, "Current Expected Credit Losses (CECL)," with guidance on:
  - Financial assets measured at amortized cost basis that are eligible for the collateral maintenance practical expedient and those that are not
  - Off balance sheet credit exposures
  - Receivables from customers
  - Securities borrowed
  - Receivables from broker-dealers and clearing organizations

- Updates to Note 9 in Exhibit 6-8 for "Receivable From and Payable to Customers"
- Additions to Chapter 5 to provide guidance for SEC-registered broker-dealers as they develop an accounting policy footnote titled "Financial Instruments – Credit Losses"

Insurance entities

On May 26, 2021, FinREC issued four working drafts addressing accounting issues for insurance entities. These drafts provide guidance on implementation of ASU 2018-12, "Financial Services – Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts." The newly released working drafts are:

- Issue 3: Market risk benefits – scope
- Issue 4D: Market risk benefits – retrospective adoption of market risk benefits guidance and the effect on purchase accounting
- Issue 6: Use of discount rates or yield curve for interest accretion on insurance liabilities under ASU 2018-12
- Issue 16: Level of aggregation for the measurement of the liability for future policy benefits

Comments were due July 29, 2021. As finalized, the text has been included in the life and health insurance entities A&A guide dated Oct. 1, 2021.

New and revised TQAs

Accounting for certain grants received under COVID-19 programs

The AICPA, on Aug. 9, 2021, issued a new Technical Question and Answer (TQA), Other Income, Section 5270.01, "Recipient Accounting for Shuttered Venue Operators Grants and Restaurant Revitalization Fund Grants Received Under the Small Business Administration COVID-19 Relief Programs." The TQA provides guidance on how a recipient should account for a Shuttered Venue Operators Grant (SVOG), which is available to private businesses and not-for-profit entities, or a Restaurant Revitalization Fund (RRF) Grant, which is available only to private business entities. The terms of these grants, which are issued under the Small Business Administration COVID-19 relief programs, do not require recipients to repay the funding as long as funds are used for eligible purposes by the dates stipulated in the programs. TQA 5270.01 presents the differing accounting models that apply, depending on whether the entity is not-for-profit or for-profit.

Healthcare entities

In December 2021, the AICPA revised Section 6400, "Health Care Entities," to conform to FASB codification revisions. Revised TQAs include:

- 6400.25 – Accounting for Transfer of Assets From Not-for-Profit to For-Profit Equity Investee
- 6400.26 – Transfer of Assets to Not-for-Profit Stockholder From For-Profit Equity Investee
- 6400.49 – Presentation of Claims Liability and Insurance Recoveries – Contingencies Similar to Malpractice
- 6400.53 – Accounting for Costs Incurred in Connection With the Implementation of Electronic Health Record Systems
- 6400.64 – Accounting for Provider Relief Fund General and Targeted Distribution Payments

In April 2021, the AICPA revised Section 6400, "Health Care Entities," of its TQAs relating to provisions of the CARES Act specific to healthcare entities. The TQAs, originally issued in 2020, help nongovernmental healthcare entities account for payments received from the CARES Act, the Provider Relief Fund, and boosted Medicare and Medicaid payments.

The revised TQAs include:

- 6400.63 – Background to Sections 6400.64-.70 – CARES Act Provisions Specific to Health Care Entities
- 6400.64 – Accounting for Provider Relief Fund General and Targeted Distribution Payments
- 6400.66 – Period of Accounting for Provider Relief Fund Phase 1 General Distribution Payments
- 6400.68 – Accounting for Payments Received Under the Medicare Accelerated and Advance Payment Program

From the Center for Audit Quality (CAQ)

ESG focus

Climate-related risk reporting requirements and considerations

On Sept. 9, 2021, the CAQ released "Audited Financial Statements and Climate-Related Risk Considerations," a document providing information on the direct and indirect impact of climate-related risks on financial statements and audits. As a foundation for upcoming regulatory changes, the document explores the current requirements under U.S. GAAP and PCAOB auditing standards for addressing climate-related risks and disclosures.

ESG reporting and assurance across S&P 500 companies

On Aug. 9, 2021, the CAQ released summary observations of the nature and extent, including any assurance obtained, of publicly available ESG reports using the most recently available data for S&P 500 companies. The summary provides additional observations focused on S&P 100 companies.

Analysis of ESG reporting

The CAQ, on April 29, 2021, published "S&P 100 and ESG Reporting," summarizing its findings from an examination of publicly available ESG information for S&P 100 companies through March 12, 2021. The CAQ reports that all companies provided some ESG information, most reported it in a separate stand-alone report, and 11 obtained assurance from a public company auditing firm for some of the information. The report shows which frameworks were most widely used and which standards were commonly referenced, information about what types of information assurance were obtained from auditors, and a description of assurances obtained from other providers such as engineering and consulting firms.

Effective governance over ESG reporting

On April 22, 2021, the CAQ and the AICPA published "Key Actions for Establishing Effective Governance Over ESG Reporting" to provide guidance on the creation of high-quality ESG disclosures. The report describes key actions to establish effective governance over ESG reporting, including:

- Conducting materiality or risk assessments to determine which ESG topics are important or material to the organization, its investors, and other stakeholders
- Implementing appropriate board oversight of material ESG matters
- Integrating and aligning material ESG topics into the enterprise risk management process
- Integrating ESG matters into the overall company strategy

According to the CAQ, "Good governance plays a critical role in a company's ability to produce high-quality, accurate and reliable information," and this document provides a starting point with actions entities can take to reach that goal.

ESG disclosure information

On Feb. 17, 2021, the CAQ and the Association of International Certified Professional Accountants issued a joint publication, "ESG Reporting and Attestation: A Roadmap for Audit Practitioners." Although written from the perspective of audit practitioners, it contains a number of data points preparers also might consider when developing their understanding of ESG disclosures, including where and how to report ESG information.

2021 "Audit Committee Transparency Barometer" report

On Nov. 10, 2021, the CAQ and Audit Analytics issued the "2021 Audit Committee Transparency Barometer," which tracks S&P 1500 proxy disclosures to evaluate transparency regarding audit committee oversight of the external auditor and other important financial reporting topics.

The CAQ notes that voluntary disclosure of audit committee oversight indicates higher levels of involvement. In addition, effective audit committee oversight enhances audit quality. This edition of the barometer reports that – as has been the case – the highest rates of disclosure relate to nonaudit services, auditor tenure, criteria considered to evaluate the audit firm, and involvement in audit partner selection. Additionally, the report highlights that cybersecurity disclosures continue to have the greatest increases year over year since 2016. The report finds that disclosures related to auditor compensation and explanations for changes in fees paid to the external auditor have the lowest rates of disclosures and provide the greatest opportunity for improvement. The publication also provides disclosure examples.

SPACs alert

The CAQ issued Alert 2021-01, "Auditor and Audit Committee Considerations Relating to Special Purposes Acquisition Company (SPAC) Initial Public Offerings and Mergers," on May 3, 2021. It describes the five phases of a SPAC life cycle and provides a listing of considerations for auditors and audit committees regarding challenges of a private company entering the public markets through a merger with a SPAC. While these considerations are intended for auditors and audit committees, members of management also might find them helpful.

Referring to the SEC statement on "Financial Reporting and Auditing Considerations of Companies Merging With SPACs," the alert repeats, "it is critical that the board of directors, audit committees (as applicable), management, and auditors of operating companies involved in a merger with a SPAC fully understand and fulfill their professional responsibilities so that companies meet their obligations under the federal securities laws and investors are provided with high quality financial reporting at the time of the merger and on an ongoing basis." To help address this responsibility, the alert lists numerous considerations related to SPAC merger transactions for auditors and audit committees. For audit committees, the alert describes considerations related to public company readiness; SPAC sponsor experience; corporate governance; accounting, reporting, and disclosure issues; and external auditor selection and oversight.

Effectiveness of management review controls

On April 21, 2021, the CAQ released "Issues Related to the Assessment of the Effectiveness of Management Review Controls: Roundtable Summary." This report summarizes the information gathered during a roundtable discussion led by the CAQ and the Financial Education & Research Foundation with preparers and auditors who did not participate in the research study on internal control over financial reporting management review controls, "Perspectives on Management Review Controls: Challenges and Solutions." The objective of the roundtable was to identify and share practices that can mitigate challenges of addressing management review controls. The report addresses planning and communication, design and precision, and operation and performance of management review controls. It identifies important best practices to address management review control challenges and provides a detailed listing of suggested actions to address challenges with management's assessment and the auditor's evaluation of the effectiveness of management review controls.

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Audit2299-007A