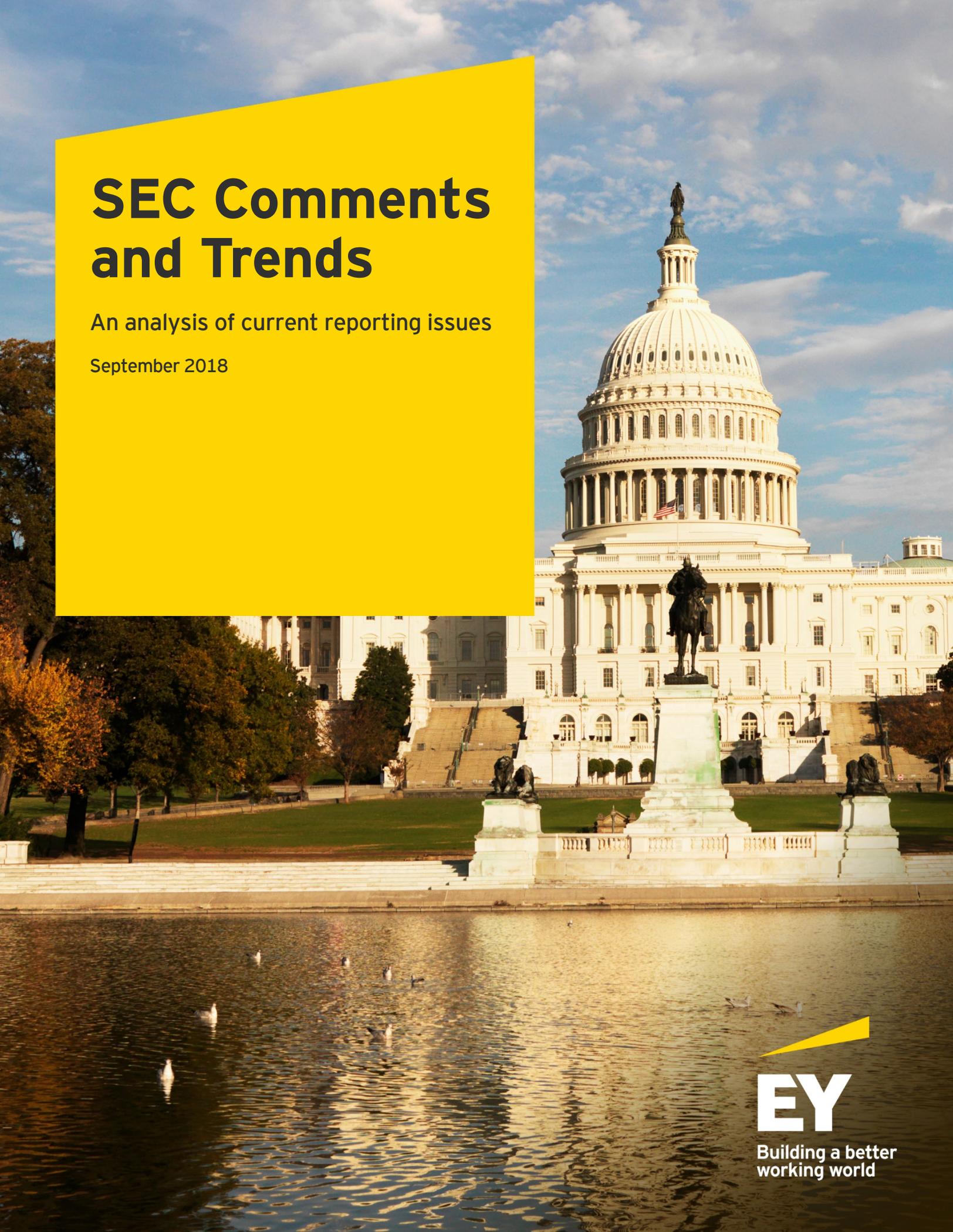


# SEC Comments and Trends

An analysis of current reporting issues

September 2018



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# To our clients and other friends

Every year, we closely monitor the Securities and Exchange Commission (SEC) staff's comments on public company filings to provide you with insights on its areas of focus. Understanding the current financial reporting landscape and the types of issues that the SEC staff is focusing on in its comments will help you as you head into the year-end reporting season.

While this publication highlights areas where the SEC staff has commented in the past, it is not intended to drive changes to your accounting or disclosure unless you determine that changes are necessary to comply with the accounting or disclosure requirements. However, the comments and trends may help you identify disclosure improvements or enhance your documentation of your accounting conclusions.

We recommend that companies refrain from making decisions about disclosures solely to avoid a comment letter. If you receive a comment letter from the SEC staff, view it as an opportunity to educate the staff about your facts and how you arrived at the conclusions leading to your disclosure, which may include clarifying your consideration of materiality. Following the best practices in Appendix D often leads to a relatively short dialogue with the SEC staff. We also note that many companies resolve a comment without changing their disclosures.

The SEC staff continues to focus on many of the same topics that we highlighted last year. The following chart summarizes the top 10 most frequent comment areas in the current and previous years.

Comment area	Ranking		Comments as % of total registrants that received comment letters*
	12 months ended 30 June		
	2018	2017	2017 and 2018
Management's discussion and analysis**	1	2	43%
Non-GAAP financial measures	2	1	47%
Fair value measurements***	3	3	17%
Segment reporting	4	4	15%
Revenue recognition	5	5	13%
Intangible assets and goodwill	6	6	11%
State sponsors of terrorism	7	8	12%
Income taxes	8	7	12%
Acquisitions and business combinations	9	9	8%
Contingencies	10	****	6%

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to registrants about Forms 10-K from 1 July 2016 through 30 June 2018. In some cases, individual SEC staff comments are assigned to multiple topics if the same comment covers multiple accounting or disclosure areas.

\*\* This category includes comments on MD&A topics, in order of frequency: (1) results of operations (20%), (2) critical accounting policies and estimates (10%), (3) liquidity matters (8%), (4) business overview (6%) and (5) contractual obligations (2%). Many companies received MD&A comments in more than one category.

\*\*\* This category includes SEC staff comments on fair value measurements under Accounting Standards Codification (ASC) 820 as well as fair value estimates, such as those related to revenue recognition, stock compensation and goodwill impairment analyses.

\*\*\*\* This topic was not among the top 10 in 2017.

Management's discussion and analysis (MD&A) is back in the top spot as the most frequent area of comment, moving slightly ahead of non-GAAP financial measures. The SEC staff also continues to question registrants' disclosures related to significant judgments and estimates, including those related to segment reporting, goodwill impairment and income taxes.

Comments issued to early adopters of the new revenue recognition standard have also focused on areas of judgment (e.g., identifying performance obligations, determining the timing of satisfaction of performance obligations, determining the amortization period of capitalized contract costs) and may indicate areas the SEC staff will focus on when reviewing the filings of registrants that adopted the standard in 2018.

The main section of this publication discusses recent matters that concern all registrants. Appendices A, B and C highlight emerging trends related to specific industries, companies filing initial public offering (IPO) registration statements and foreign private issuers, respectively. Appendix D provides an overview of the SEC staff's filing review process and best practices for responding to staff comments.

We hope you find this publication helpful. EY professionals are prepared to discuss any concerns or questions you may have.

*Ernst + Young LLP*

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# Management's discussion and analysis

## Results of operations

### *Summary of issues noted*

The SEC staff often requests that registrants explain the results of their operations with greater specificity, including identifying underlying drivers for each material factor that affected their earnings or is reasonably likely to have a material effect on future earnings. In addition to commenting on the analysis of changes in revenue, the SEC staff has been commenting on significant components of expenses and provisions.

The SEC staff also has increased its focus on performance metrics, including whether registrants have disclosed key metrics used by management and how those metrics correlate to material changes in the results of operations.

### *Analysis of current issues*

Item 303(a)(3) of Regulation S-K provides general instructions for preparing MD&A disclosures about the results of operations. The SEC staff often asks registrants to provide a more detailed discussion about their results of operations, including requesting that they:

- ▶ Describe any unusual or infrequent events or transactions, or any significant economic changes, that materially affect income from continuing operations, as well as the extent to which income was affected (e.g., significant events that have been disclosed in the press but not disclosed in an SEC filing)
- ▶ Describe any other significant components of revenue or expense necessary to understand the results of operations (such as components of cost of sales)
- ▶ Describe any known trends or uncertainties that have had or are reasonably likely to have a material effect on sales, revenue or income from continuing operations (such as uncertainties arising from foreign operations in countries subject to political or financial risk)
- ▶ Discuss how much of any material increase in net sales or revenue is due to business combinations, increased sales volume, introduction of new products or services, or increased sales prices and quantify each factor's effect, if possible
- ▶ Discuss segment information needed to understand their results of operations, including the effect that the performance of a particular product line may have had, in addition to discussing the registrant as a whole
- ▶ Discuss the reasons for a significant change in the effective income tax rate and whether those drivers are expected to affect the future income tax rate (refer to the income taxes section for further discussion)

The SEC staff typically requests that registrants quantify the effects of factors that contributed to material period-to-period changes, including the underlying business or economic factors and material offsetting factors, and provide a more granular discussion of the effects. For example, when a registrant discloses that two or more factors contributed to a material period-to-period change in a financial statement line item, the SEC staff often requests that the registrant quantify and analyze each factor's effect.

**Example SEC staff comment: Results of operations – quantification of factors**

We note that your comparative discussions of costs and expenses identify multiple variables as the reasons for the period-to-period changes in your operating results. However, you do not quantify the impact of each of these variables.

Please revise to quantify the impact of each material factor that you discuss to provide your readers with better insight into the underlying reasons behind the changes in your results. Refer to Instruction 4 to Item 303(a) of Regulation S-K, Section III.D of Release No. 33-6835 and Section III.B of Release No. 33-8350.

Some of the factors that may cause material period-to-period changes in revenue and operating costs at a registrant's reportable segments include foreign currency fluctuations and changes in the macroeconomic environments around the world. The SEC staff expects registrants to quantify any material effect of such factors on the reportable segment.

The SEC staff has also requested that companies provide forward-looking information about known trends and uncertainties. This information is required for trends and uncertainties that have had or are reasonably likely to have a material effect on revenues or income from continuing operations. In evaluating this requirement, the registrant must determine whether the trend or uncertainty is reasonably likely to occur. If it isn't, no disclosure is required. If the registrant cannot make that determination, it must assume that the trend or uncertainty will occur, and it must disclose that item in MD&A, unless it is not reasonably likely to have a material effect.

When material effects on results of operations are ascribed to an increase (or decrease) in headcount or other internal initiatives (e.g., implementation of a new information technology system), the SEC staff may ask registrants to discuss their expectations about ongoing investments in these initiatives. When registrants discuss changes in laws or regulations, foreign exchange rates or economic conditions (e.g., increasing interest rates), the SEC staff may ask about the expected effects of these items on revenues and income in future periods.

**Example SEC staff comment: Results of operations – known trends and uncertainties**

We note a substantial increase in your allowance for doubtful accounts year over year. And, we note a further increase in the first quarter ended March 31, 2017.

Please expand MD&A and Risk Factors in future filings to discuss all known material trends, events or uncertainties that have had or are reasonably expected to have a material impact on your financial condition and results of operation. Refer to Item 303(a)(3) of Regulation S-K and SEC Release No. 33-8350.

To assess the completeness of MD&A disclosures in a registrant's periodic reports (e.g., Forms 10-K, 10-Q), particularly related to material trends or uncertainties, the SEC staff may also listen to a registrant's earnings calls and read other relevant information (e.g., earnings releases, investor presentations). The SEC staff has often asked registrants to expand their MD&A disclosures when a material trend or uncertainty is not discussed in MD&A but the entity had addressed it in an earnings release or call.

**Example SEC staff comment: Results of operations – Expanding MD&A based on a known material trend discussed in earnings release**

We note you highlight in your earnings release that 2017 was “Another Year of Significant Cost Reductions.” Please provide a more detailed discussion of the specific components of costs of services in MD&A that management believes can be reduced through the Company’s ongoing cost reduction efforts.

*Significant components of expense and changes in reserve balances*

The SEC staff has asked registrants to expand their discussions about significant components of operating expenses, such as costs of sales. In their segment discussions, registrants often describe only changes in revenue and operating income and do not directly explain the changes in significant operating expenses. The SEC staff frequently asks registrants to quantify and discuss separately the significant components of operating expenses that have affected segment operating income. The SEC staff believes this information helps investors better understand a registrant’s business.

In addition, the SEC staff continues to ask for additional information and disclosure about material provisions or reversals affecting reserve accounts (e.g., bad debt allowance, inventory reserves, sales return reserves) as well as their effects on the results of operations.

**Example SEC staff comment: Results of operations – changes in reserve accounts**

Please expand your disclosures to explain the reasons for the changes in your provision for credit losses on loans receivable recorded for each period presented. See Item 303 of Regulation S-K and SEC Release No. 33-8350.

*Key financial and operating metrics*

The SEC staff continues to believe that key financial and operating metrics can be useful for investors to assess operating performance. SEC Chief Accountant Wes Bricker has emphasized the importance of having effective disclosure controls and procedures with respect to these performance metrics. “Similar to non-GAAP financial reporting, key operating metrics and forecasts may also be distorted via bias – for example, painting a potentially misleading picture – error or fraud, all of which undermine the credibility of the reporting. Therefore, it is important that companies proactively and thoughtfully address risks to their reporting,” Mr. Bricker said in a speech in May 2017.

When a registrant uses a key metric to discuss operating results in MD&A, the SEC staff frequently requests that it:

- ▶ Define the metric, especially when a registrant’s definition differs from the definition commonly used in its industry
- ▶ Discuss how the metric is calculated

- ▶ Provide robust disclosures explaining any changes made to the calculation of the metric
- ▶ Discuss any limits on the usefulness of the metric (e.g., individuals may be counted more than once in an "average monthly users" metric)
- ▶ Consider providing information about the metric on a disaggregated basis, such as by segment, geography or revenue stream (e.g., breaking down same-store sales between e-commerce and in-store sales)
- ▶ Clearly explain how the metric or period-to-period change in the metric links to operating results to reveal a trend (e.g., using the increase in the number of customers to explain revenue growth)

To help investors view the registrant through the eyes of management, the SEC's guidance on MD&A suggests that the registrant disclose in MD&A the key performance indicators, financial or nonfinancial, that are used to manage its business. Key performance metrics vary by industry. For example, retail companies use same-store sales and store openings and closings, while social networking and online gaming companies typically focus on the number of monthly or daily users. The SEC staff may ask a registrant to disclose key performance indicators in its SEC filings if the registrant cites the indicator on its website, in a press release or analyst presentation or in another setting.

**Example SEC staff comment: Results of operations – missing key financial metrics**

We note your reference, both in your risk factor disclosures and on your earnings calls, to the impact of capacity utilization rates on your financial condition and results of operations. To the extent that utilization rates are a key performance indicator used in managing your business, please include a discussion of this measure along with comparative period amounts or explain why you do not believe this disclosure is necessary.

Refer to Section III.B.1 of SEC Release No. 33-8350.

The SEC staff recognizes the value of using an operating metric in MD&A to help explain operating results. However, the staff has asked for clarification when it believes that a registrant's use of such metrics without the appropriate context is potentially misleading and does not appropriately explain any changes in income statement line items. For example, if a company discloses that it has 10 million total users and expects the number to grow 12%, but doesn't explain that the majority of them are non-paying, investors may incorrectly expect a direct correlation between total user growth and profitability.

**Example SEC staff comment: Results of operations – key financial metrics**

Your disclosure indicates that the “registered device user metric” is an indicator of the potential size and growth of your paid user community.

To the extent that a prior user of a device continues to be included in this count, please tell us how counting such a user provides an indication of the potential size or growth of your paid user community. Please also explain why this metric represents your potential paid user community when some of the users may not have used your device for an extended period of time.

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Compendium of significant accounting and reporting issues, [2017 AICPA Conference on Current SEC and PCAOB Developments](#)

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## Critical accounting estimates

### *Summary of issues noted*

The SEC staff's comments have frequently targeted repetitive discussions about critical accounting estimates in MD&A. The SEC staff has reminded registrants that MD&A should supplement but not repeat the disclosures in the significant accounting policies note to the financial statements. The SEC staff often asks registrants to focus their MD&A discussion of critical accounting estimates on the quality and variability of management's most significant judgments and assumptions.

### *Analysis of current issues*

Critical accounting estimates are those that are most important to the financial statement presentation and that require the most difficult, subjective and complex judgments. SEC Financial Release No. 72, *Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations*, (FRR-72) reminds registrants that MD&A rules require disclosure of critical accounting estimates and assumptions when both of the following conditions are met:

- ▶ The nature of the estimates or assumptions is material because of the levels of subjectivity and judgment needed to account for matters that are highly uncertain and susceptible to change.
- ▶ The effect of the estimates and assumptions is material to the financial statements.

The SEC staff has noted that registrants' disclosures about critical accounting estimates often are too general and should provide a more robust analysis than what is in the significant accounting policies note to the financial statements. The SEC staff has commented that there are numerous examples of portions of the significant accounting policies note being repeated verbatim in MD&A. While accounting policies in the notes to the financial statements generally describe the method used to apply an accounting principle, the discussion in MD&A should provide more insight into the uncertainties involved in applying the principle at a given time and the variability that is reasonably likely to result from its application.

### **Example SEC staff comment: Duplicative disclosure about critical accounting estimates**

The disclosure of critical accounting policies within MD&A appears to duplicate your accounting policy disclosure in the notes to your financial statements, and it does not provide investors with a robust discussion of your critical estimates by focusing on the assumptions and uncertainties that underlie the impairment analysis of your most significant asset.

Please modify the MD&A disclosure to address the specific methods, assumptions and estimates used in your critical accounting estimate. If you prefer to include this disclosure elsewhere in your filing, such as an expanded disclosure in the notes to your financial statements, please consider including a simple cross-reference within your MD&A to avoid repetition.

Disclosures about critical accounting estimates should focus on the quality and variability of management's judgments.

Registrants can consider including in MD&A a cross-reference to the footnote disclosure about significant accounting policies. However, they should expand the MD&A disclosure to (1) address why the accounting estimate or assumption bears the risk of change and (2) analyze the following, if material:

- ▶ How the registrant arrived at the estimate/assumption
- ▶ How accurate the estimate/assumption has been in the past
- ▶ How much the estimate/assumption has changed in the past
- ▶ Whether the estimate/assumption is reasonably likely to change in the future

Because critical accounting estimates and assumptions are based on highly uncertain matters, the SEC staff believes that registrants also should consider analyzing their sensitivity to change based on reasonably likely outcomes that could have a material effect on the financial statements. The SEC staff believes that registrants should provide quantitative information in addition to qualitative information when it is reasonably available and material.

The SEC staff may request enhancements to the MD&A discussion of specific critical accounting estimates, which we discuss separately in this publication (e.g., measurement of accounts receivable, realizability of deferred tax assets, goodwill impairment).

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## Liquidity and capital resources

### *Summary of issues noted*

The SEC staff may request enhanced disclosures in the liquidity and capital resources section of MD&A, particularly when there are trends or uncertainties affecting liquidity. Such requests may focus on:

- ▶ Sources and uses of cash and the availability of cash to fund liquidity needs
- ▶ Transparency in the contractual obligations table and its footnotes about interest payments and other items

Further, the SEC staff may request more comprehensive disclosures about alternative sources of funding and material debt covenants when there is an elevated risk of default or when management has concluded it is reasonably likely that covenants will not be complied with in the future.

### *Analysis of current issues*

#### *General disclosures*

Items 303(a)(1) and (2) of Regulation S-K require that a registrant discuss known material trends, demands, commitments, events or uncertainties that are reasonably likely to affect (either favorably or unfavorably) liquidity or capital resources. For example, if a registrant expects growth in the business from a recently completed acquisition, the SEC staff may ask the registrant to discuss the reasonably likely increase or decrease in liquidity that is expected to be material.

The SEC staff also requests that registrants expand MD&A to include a meaningful analysis and discuss the material components to explain the variability of cash flows. For example, the SEC staff often challenges the discussion about cash flows that recites items that are readily apparent from the statement of cash flows (e.g., changes in working capital) but does not provide analysis about the underlying drivers for material changes.

#### **Example SEC staff comment: Changes in operating cash flows**

Your discussion of net cash provided by operating activities does not appear to contribute substantively to an understanding of your historical cash flows. When preparing the discussion and analysis of operating cash flows, you should address material changes in the underlying drivers that affect these cash flows. These disclosures should include a discussion of the underlying reasons for changes in working capital accounts that affect operating cash flows.

The SEC staff also has requested that registrants disclose:

- ▶ Whether identified trends will continue, and if so, how long they will continue, as well as steps the registrant is taking to address the trends, including plans to remedy any identified material deficiency in short- or long-term liquidity
- ▶ An analysis of all internal and external sources of liquidity, beyond cash on hand, as of the balance sheet date

When there is a heightened risk of debt default, the SEC staff may request enhanced disclosures about debt covenants and the registrant's compliance with them.

- ▶ Amounts outstanding and available at the balance sheet date under each source of liquidity, with a comparison to cash needs over the next 12 months, including any significant planned capital expenditures
- ▶ The sufficiency of the amount available under an existing short-term credit arrangement, the anticipated circumstances requiring its use, any uncertainty surrounding the ability to access funds when needed and the implications of not being able to access the arrangement

**Example SEC staff comment: Expected sources and uses of cash over the short- and long-term period**

We note your disclosure that you “currently have the ability to raise capital pursuant to an effective shelf registration statement” and that in the future, if your operations do not become cash flow positive, you may seek equity investments.

Please revise your future filings as appropriate to discuss your liquidity sources and requirements on a short- and long-term basis; specifically addressing your anticipated sources of capital necessary to achieve your business plan. If your primary anticipated liquidity source is through equity sales, please address any factors that could affect the amount of cash you could raise given the limited authorized shares you have remaining.

When there is a heightened risk of debt default (e.g., adverse trends in cash flows or operating results, recent covenant waiver requests, significant amount of debt maturing within 12 months), the SEC staff requests enhanced disclosure about alternative sources of funding, debt covenants and the potential risks and effects of noncompliance on the registrant's financial condition and liquidity. Specifically, the SEC staff may request the following types of disclosure:

- ▶ Alternative sources of funding to refinance existing debt obligations
- ▶ Specific terms of material debt covenants and whether the registrant is in compliance with the covenants
- ▶ Actual quantitative ratios or amounts compared with required minimum/maximum values contained in debt covenants, along with explanations of how such ratios or amounts are determined and their relationship to amounts reported under US GAAP
- ▶ The nature of waivers or modifications of existing debt covenants obtained to cure or prevent potential violation(s), including how long any waivers apply and a description of the covenant
- ▶ Disclosure of the likelihood of violating financial covenants in the future

**Example SEC staff comment: Supplemental disclosures when dealing with elevated risk of debt default**

You disclose throughout your filing several instances of debt defaults and covenant violations, waivers of violations, and amendments to the terms of your debt agreements, such as the changes made to your revolving credit facility debt covenant ratios disclosed on page XX.

Please revise your MD&A to elaborate on the steps you are taking to avoid a breach of your debt covenants, the impact or reasonably likely impact of a breach on your financial condition or operating performance, and alternate sources of funding to refinance resulting obligations.

Also tell us and disclose whether there are cross default provisions under any of your existing debt obligations and quantitatively disclose the required and actual debt covenant ratios.

*Contractual obligations*

Item 303 of Regulation S-K requires registrants (other than smaller reporting companies, issuers of asset-backed securities and registered investment companies) to provide tabular presentations of contractual obligations as of the end of the most recent fiscal year.

The goal of the contractual obligations table is to present a meaningful snapshot of the cash requirements arising from such obligations. The MD&A rules permit flexibility so that the presentation can reflect the information in a way that is suitable to a registrant's business. Registrants should develop a presentation that is clear and understandable and that appropriately reflects the categories of obligations that are meaningful in light of their capital structure and business.

Uncertainties about what to include in the table and how to allocate amounts to the required periods should be resolved consistent with the purpose of the disclosure. Registrants should consider providing narrative disclosure, in addition to the table and related footnotes, to promote an understanding of the tabular data.

The SEC staff has questioned the completeness of items included in registrants' contractual obligations tables and has asked those companies to provide the reasons for excluding certain items from the table. Most notably, the SEC staff has asked companies to include amounts for future interest payments in the contractual obligations table or a footnote to the table, if material. The SEC staff also has asked registrants to disclose reasons why interest on variable debt is not included in their contractual obligations table. When interest rates are variable, registrants should also describe the assumptions that were used to estimate future payments.

**Example SEC staff comment: Contractual obligations**

We note that your disclosure of long term debt in the table of contractual obligations includes interest on your fixed rate financing but does not include interest on variable rate debt. Please revise to disclose the estimated cash requirements for interest on your variable debt obligations, including underlying assumptions used to estimate the future interest payments, or tell us why such disclosure is not necessary.

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# SEC reporting issues

## Non-GAAP measures

### *Summary of issues noted*

While the SEC staff has been less vocal on non-GAAP financial measures in 2018, it continues to issue comments on this topic. These comments are consistent with what we observed in the prior year after the SEC staff made its guidance on non-GAAP measures more explicit in an update to its Compliance and Disclosure Interpretations (C&DIs) in May 2016.

The SEC staff has asked registrants to explain how their use of non-GAAP financial measures complies with the C&DIs or to change their presentation of items, including:

- ▶ Non-GAAP financial measures that tailor GAAP recognition and measurement principles, don't include the same items in all periods, don't treat similar gains and losses consistently or exclude normal cash operating expenses from performance measures
- ▶ Non-GAAP financial measures that are presented more prominently than GAAP measures or disclosures that don't appear to comply with Item 10(e) of Regulation S-K (e.g., presenting a measure that could be misleading, omitting disclosure of the measure's usefulness to investors or management, removing cash-settled charges from liquidity measures, labeling recurring items as nonrecurring)

Many of the SEC staff comments have focused on registrants' use of non-GAAP financial measures in earnings releases and other information (e.g., websites, investor presentations) in addition to their SEC filings.

### *Analysis of current issues*

The C&DIs provide explicit guidance on uses of non-GAAP financial measures that the SEC staff believes could be misleading. A non-GAAP financial measure may be considered misleading if it (1) is presented inconsistently in different fiscal periods or if similar gains and losses are treated differently; (2) excludes normal, recurring cash operating expenses from performance measures; or (3) tailors GAAP recognition and measurement principles, such as accelerating deferred revenue. In its comment letters, the SEC staff has focused on all three areas.

### *Inconsistent presentation*

In the C&DIs, the SEC staff said that presenting a non-GAAP financial measure that adjusts a particular charge or gain in the current period but doesn't adjust similar charges or gains in prior periods could violate Regulation G unless the change is disclosed and the reasons for it are explained. The SEC staff has asked registrants how they define specific non-GAAP measures and challenged whether unusual gains have been eliminated consistently with unusual charges or losses.

#### **Example SEC staff comment: Inconsistent presentation**

We note that you disclose the non-GAAP measure “Adjusted earnings,” which excludes pension settlement charges, merger and restructuring charges and abandonment and impairment charges. Considering you have not provided any adjustments to exclude net gains on asset sales, please advise us how you have considered Question 100.03 of the updated C&DIs issued on May 17, 2016.

#### *Exclusion of normal, recurring cash operating expenses*

In the C&DIs, the SEC staff said that non-GAAP performance measures could be considered misleading if they exclude normal, recurring cash operating expenses necessary to operate the registrant’s business. The SEC staff has asked registrants whether non-GAAP performance measures exclude recurring charges such as restructuring charges and litigation costs that should be included as normal, cash operating expenses.

#### **Example SEC staff comment: Exclusion of normal, recurring cash operating expenses**

We note several items in the reconciliation of earnings before interest, tax, depreciation and amortization (EBITDA) to adjusted EBITDA remove recurring cash operating expenses, such as professional fees and management fees and expenses. Considering these adjustments include recurring cash operating expenses, tell us how your presentation complies with the May 17, 2016 updated C&DIs on Non-GAAP financial measures.

#### *Tailoring GAAP recognition and measurement principles*

In the C&DIs, the SEC staff clarified that non-GAAP performance measures that accelerate the recognition of revenue to the time of sale or customer billing but under GAAP would be recognized ratably over the performance period or that use other accounting methods not allowed under GAAP (e.g., proportionate consolidation) may be misleading.

While the SEC staff initially focused on revenue when asking about compliance with this interpretation, the SEC staff has broadened its approach and challenged other ways registrants modify GAAP recognition and measurement principles in calculating non-GAAP financial measures such as the use of proportionate consolidation for equity investees, accounting for operating leases as capital leases or eliminating the provision for loan losses. We expect this issue to continue to receive attention if companies present non-GAAP financial measures that unwind the effects of new accounting standards (for purposes other than providing transition disclosures).

The SEC staff may object to adjustments that unwind the effects of new accounting standards for reasons other than providing transition disclosures.

**Example SEC staff comment: tailoring recognition of allowance for loan losses**

We note the disclosure of the non-GAAP measure “adjusted allowance for loan losses/non-acquired loans held for investment.” We also note you eliminated the allowance for loans losses attributable to XX. Tell us how you considered whether the non-GAAP measure uses an individually tailored recognition and measurement method, which could violate Rule 100(b) of Regulation G. Please refer to Question 100.04 of the Compliance and Disclosure Interpretations for guidance.

*Compliance with Item 10(e) of Regulation S-K*

Item 10(e)(1)(i)(A) of Regulation S-K requires a presentation, with equal or greater prominence, of the most directly comparable financial measure or measures calculated and presented in accordance with GAAP. However, the SEC staff does not believe that a registrant can comply with this requirement unless a GAAP measure precedes the related non-GAAP measure either in an SEC filing or earnings release.

The prohibition on presenting non-GAAP financial measures with greater prominence than GAAP measures applies to both the order of presentation and the degree of emphasis. For example, the SEC staff has questioned discussions of non-GAAP financial measures that precede the discussion of the corresponding GAAP measures, use bold or larger font or significantly exceed the length of the discussion of the corresponding GAAP measures.

**Example SEC staff comment: Prominence of non-GAAP measures**

We note that you present non-GAAP earnings and non-GAAP margin before the most directly comparable GAAP measures. Your presentation appears to give greater prominence to the non-GAAP measures than to the comparable GAAP measures, which is inconsistent with the updated C&DIs issued on May 17, 2016. Please review that guidance when preparing future earnings releases.

The SEC staff also has asked registrants to clarify and expand their disclosures to discuss how a particular measure is useful to investors and how management uses it. Often, these disclosures are boilerplate or too general to help readers understand how they should use a particular measure.

If a registrant cannot explain how a measure is useful to investors, or if the SEC staff believes the presentation could be misleading, the SEC staff has asked registrants to expand the disclosure or remove the non-GAAP measure. Additionally, the SEC staff has questioned the usefulness of adjustments that do not appear to be consistent with the purpose of the measure described by the registrant. When disclosing non-GAAP financial measures, registrants also should consider the following areas of frequent SEC staff comment:

- ▶ The labeling of a non-GAAP financial measure that is similar to a standard measure, but adjusted to some extent, should clearly indicate that fact. For example, a measure that includes adjustments to the standard definition of EBITDA should not be labeled “EBITDA.”

- ▶ Adjustments to non-GAAP measures that are labeled as nonrecurring should only comprise items that are infrequent or unusual in nature, as required by Item 10(e)(1)(ii)(B) of Regulation S-K. If the adjusted item has occurred within the past two years or is likely to recur within two years, it should not be characterized as nonrecurring.

**Example SEC staff comment: Usefulness of a non-GAAP measure**

We note your disclosure of the non-GAAP measure “adjusted net income” provides a meaningful comparison of financial performance between years and transparency in your operating results. However, your current disclosure is too generic in terms of describing how you use it and why it is useful to investors. Please revise your disclosure to provide more detail regarding how you use it and its usefulness to investors.

In the C&DIs, the SEC staff also noted that constant currency measures are considered non-GAAP financial measures and said that registrants should present the historical amounts and describe their process for calculating constant currency amounts in lieu of a numeric reconciliation of the non-GAAP metric. The SEC staff has commented on registrants’ use of constant currency measures and compliance with its interpretation.

**Example SEC staff comment: Constant currency measures**

You disclose your results on a constant currency basis, which appear to be non-GAAP financial measures. In future periodic filings, please describe the process for calculating the currency effects, including which period’s exchange rate is used. Also provide such disclosure in your interim periodic filings and quarterly earnings announcements.

Registrants must present non-GAAP financial measures with quantitative reconciliations to the most directly comparable GAAP measures. This requirement also applies to forward-looking non-GAAP measures if the forward-looking GAAP measure is reasonably available. If a comparable GAAP measure isn’t available, the SEC staff expects registrants to disclose why the reconciliation is not presented. The SEC staff has objected to registrants presenting a full non-GAAP income statement as a form of reconciliation because this makes the non-GAAP information more prominent. The SEC staff has also objected to registrants presenting reconciliations that begin with the non-GAAP information.

**Example SEC staff comment: full non-GAAP income statement**

You present a full non-GAAP income statement when reconciling non-GAAP measures to the most directly comparable GAAP measures. Please be advised it is not appropriate to present a full non-GAAP income statement for purposes of reconciling non-GAAP measures to the most directly comparable GAAP measure. Please revise and reconcile without presenting a full non-GAAP income statement. See Question 102.10 of the Compliance and Disclosure Interpretations issued on May 17, 2016.

*Liquidity versus performance measures*

Non-GAAP financial measures may be presented as performance measures, liquidity measures or both. When a registrant uses a non-GAAP measure as both a performance and liquidity measure, the registrant should include separate reconciliations and disclosures for each type of measure. For example, a registrant should reconcile EBITDA to both net income and cash flows from operations if EBITDA is presented as both a performance measure and a liquidity measure.

The SEC staff has asked registrants to revise future disclosures to comply with the Regulation S-K requirements for liquidity measures. Registrants cannot present non-GAAP liquidity measures on a per-share basis, and they cannot adjust liquidity measures to remove charges or liabilities that require or will require cash settlement.

**Example SEC staff comment: Non-GAAP liquidity measures**

It appears that your presentation of operating cash flow per share is not consistent with the guidance in our response to Question 102.05 of the updated C&DIs issued on May 17, 2016. Please review this guidance and tell us how you intend to revise your future earnings releases.

**EY resources**

[Technical Line, A closer look at the SEC's staff scrutiny of non-GAAP financial measures](#)  
[2017 SEC annual reports – Form 10-K](#)

## Executive compensation disclosures

### *Summary of issues noted*

The SEC staff focuses its reviews on registrants' compensation discussion and analysis (CD&A) in an effort to promote more direct, specific and clear executive compensation disclosures. The CD&A should explain how and why a registrant's compensation committee establishes executive compensation policies and reaches specific executive compensation decisions. The SEC staff may perform these reviews separately from or in conjunction with its review of other sections of a company's filing.

The SEC staff recently has commented on:

- ▶ Effects of performance criteria and targets, and shareholder advisory votes on compensation decisions
- ▶ Requirements to update executive compensation disclosures in registration statements

### *Analysis of current issues*

Item 402 of Regulation S-K requires registrants to include disclosures related to director and executive officer compensation in most proxy or information statements, Form 10-K filings and various registration statements.

The SEC staff has asked registrants to provide details on individual and corporate performance criteria and targets, both quantitative and qualitative, for each named executive. Such details include how the targets were met and how meeting those targets aligns with the overall strategy of the company. Registrants are not required to disclose the targets if doing so would result in competitive harm. A registrant that doesn't disclose targets must disclose how difficult it will be for the executive or how likely it will be for the registrant to achieve those targets.

#### **Example SEC staff comment: Executive compensation disclosures**

We note that the corporate performance measures used to determine bonus awards under your incentive plan were consolidated revenue and adjusted earnings per share (EPS). In future filings, please clearly disclose the minimum, target and maximum for both the performance goals and payout levels for your incentive plan. The grants of plan-based awards tables should include threshold, target and maximum estimated future payouts under equity and non-equity incentive plans. Refer to Item 402(b)(2)(v) of Regulation S-K. To the extent you believe that disclosure of the targets is not required because it would result in competitive harm such that you may omit this information under Instruction 4 to Item 402(b) of Regulation S-K, please provide a detailed explanation of such conclusion.

Item 402(b) of Regulation S-K requires a registrant to disclose how the results of the most recent shareholder advisory vote on executive compensation were considered in determining compensation policies and decisions. The SEC staff has asked registrants to disclose in future filings the results of shareholder advisory votes and their effect on executive compensation.

**Example SEC staff comment: Shareholder advisory vote**

In future filings, please disclose whether and, if so, how the compensation committee has considered the results of your most recent shareholder advisory vote on executive compensation in determining compensation policies and decisions.

The SEC staff also may request that a registrant clarify the factors that its compensation committee considered when it exercised its discretion in granting equity awards.

***EY resources***

*[2018 proxy statements: An overview of the requirements and observations about current practice](#)*

## SAB 74 disclosures

### *Summary of issues noted*

With registrants preparing to adopt new standards on leases and credit impairment, and in some cases the new revenue recognition standard, SEC officials have continued to emphasize the disclosures registrants should provide to comply with Staff Accounting Bulletin (SAB) Topic 11.M (issued as SAB 74) and the announcement the SEC staff made in 2016 about its expectations.

The SEC staff has been closely monitoring registrants' disclosures about the revenue standard, which was effective 1 January 2018 for calendar-year registrants that aren't emerging growth companies using private company adoption dates, and we expect the SEC staff to closely monitor disclosures related to the pending adoption of the leases and credit impairment standards.

### *Analysis of current issues*

The SEC staff expects registrants to include a description of the process they are using to assess the effect of a new standard, indicate where they are in the implementation process and what matters still need to be addressed, and identify the additional steps they plan to take.

The SEC staff also expects a registrant's disclosures to evolve as the effective date of a standard nears, and the registrant makes progress on its implementation plan. That is, the SEC staff expects a registrant's disclosures to be more specific each quarter. It is important for management to consider these expectations when developing a company's disclosures and discuss them with the audit committee each quarter.

If a registrant does not know or cannot reasonably estimate the effect that adopting a new standard will have on its financial statements, it should make a statement to that effect and consider providing qualitative disclosures to help a user assess the potential significance on the financial statements. These qualitative disclosures should include a description of the new standard's effect on the registrant's accounting policies and provide a comparison to the registrant's current accounting policies.

For example, for the new revenue standard, the SEC staff has said that a registrant should consider the full scope of the new standard, including presentation in the financial statements and disclosures in the notes to the financial statements, when evaluating the standard's effect on its financial statements.

### **Example SEC staff comment: SAB 74 disclosure**

You state that you are in the process of evaluating the impact that ASC 842, *Leases*, will have on your consolidated financial statements. Please revise to provide a qualitative discussion of the potential impact that this standard will have on your financial statements when adopted. In this regard, include a description of the effects of the standard that you expect to apply and a comparison to your current lease accounting and disclosure policies. Describe the status of your process to implement the new standard and the significant implementation matters yet to be addressed. In addition, to the extent that you determine the quantitative impact that adoption of ASC 842 will have on your results or financial position, please also disclose such amounts.

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The SEC expects a registrant's disclosures to evolve and be more specific as the effective date of a standard nears.

## Exhibits and signatures

### *Summary of issues noted*

The SEC staff has questioned the completeness and adequacy of exhibits, consents, auditor's reports, management signatures and certifications filed by registrants as required by various rules and regulations. Although deficiencies in these items may seem inconsequential, they may require registrants to amend their filings.

### *Analysis of current issues*

#### *Compliance with Item 601(b)(10) of Regulation S-K*

When a registrant has discussed significant transactions or agreements in its disclosures, the SEC staff has asked why the related contracts were not filed as exhibits under Item 601(b)(10) of Regulation S-K. In addition, the SEC staff has asked registrants to file missing schedules, exhibits or appendices of material contracts (e.g., a credit agreement should be filed with all of its schedules, exhibits and appendices). Registrants often can provide the missing information in a subsequent filing. That is, they don't have to amend the original filing.

#### **Example SEC staff comment: Compliance with Item 601(b)(10)**

In future filings, please file all related party contracts as exhibits, consistent with Item 601(b)(10). If you do not believe that any of these related contracts you reference in your filing are required to be filed, please provide us with that analysis at this time.

### *Consents and auditors' reports*

Item 601 of Regulation S-K requires registrants to file the consents of experts (e.g., auditors) and counsel as exhibits to various forms filed with the SEC. Independent registered public accounting firms must consent to the use of their names and related reports in Securities Act registration statements. The SEC staff has issued comments when such required consents (1) are missing from the filing, (2) omit the signature of the accounting firm or the date of the consent, or (3) refer to the incorrect auditor's report or periods covered by that report.

#### **Example SEC staff comment: Missing consent**

It appears your Form 10-K is incorporated by reference into Form S-8 filed XXX. Please tell us why you did not file an auditor's consent related to the use of the audit report. Refer to Item 601(23) of Regulation S-K.

Registrants should make sure that the "Report of Independent Registered Public Accounting Firm" also includes the signature and location of the accounting firm and appropriately identifies all periods, financial statements and schedules that have been audited.

Management and the audit committee should also confirm that the auditor has changed its auditor's report to comply with a new Public Company Accounting Oversight Board (PCAOB) standard that requires auditors to include significantly more information in their reports. While certain requirements are already in effect, the requirement to report critical audit matters is being phased in over the next few years.

### *Section 302 certifications*

The management certification required under Section 302 of the Sarbanes-Oxley Act must be filed as Exhibit 31 to the Form 10-K. The specified form of the Section 302 certification must be filed exactly as specified in Item 601(b)(31)(i) or (ii) of Regulation S-K. Separate certifications must be filed by the principal executive officer and principal financial officer.

The SEC staff frequently has asked registrants to correct these certifications by refiling the entire report in an amendment (i.e., not simply filing a revised certification). When preparing officer certifications, registrants should:

- ▶ Follow the exact form specified by Item 601(b)(31) of Regulation S-K
- ▶ Not include the certifying individual's title in the first line of the certification
- ▶ Include the required language on internal control over financial reporting (ICFR) in the fourth paragraph of the certification when management's report on ICFR is included in the Form 10-K (this language may be omitted during the transition period allowed for newly public companies to comply with Item 308(a) of Regulation S-K)
- ▶ Include a conformed signature of the signing officer, the officer's job title and the date the certification was signed at the bottom of the certification

#### **Example SEC staff comment: Section 302 certifications**

We note that your certification filed on Exhibit 31.1 does not include the signature of the officer completing the certification, the job title(s) of the officer and the date that the certification was signed. Please file an amended Form 10-K to revise this certification accordingly. Refer to the guidance in Item 601(B)(31) of Regulation S-K.

### *Form 10-K signatures*

General Instruction D of Form 10-K requires the annual report to be signed by the registrant and on the registrant's behalf by (1) its principal executive officer(s), (2) its principal financial officer(s), (3) its controller or principal accounting officer and (4) a majority of the board of directors or others acting in a similar capacity. If an officer signs the filing in multiple capacities (e.g., the chief financial officer is also the principal accounting officer), his or her signature line should indicate all such roles.

The SEC staff requires registrants to include the signature of the person serving as the controller or principal accounting officer or indicate who signed the report in that capacity. It's also important that the Form 10-K include officers' signatures on behalf of the registrant, as well as in their capacity as officers. Officers sometimes incorrectly sign only on behalf of the registrant and not individually, or vice versa.

**Example SEC staff comment: Form 10-K signatures**

Please note that your annual report on Form 10-K must be signed by your controller or principal accounting officer. Any person who occupies more than one of the specified positions should indicate each capacity in which he or she signs the report. Please refer to General Instruction D(2) of Form 10-K and advise.

***EY resources***

[2017 SEC annual reports – Form 10-K](#)

## Internal control over financial reporting and disclosure controls and procedures

### *Summary of issues noted*

ICFR continues to be an area of significant focus of the SEC staff. The SEC staff has questioned the following areas related to ICFR and disclosure controls and procedures:

- ▶ The nature and timely identification of material weaknesses
- ▶ The implications for ICFR when a registrant discloses an error correction, regardless of whether it is material
- ▶ The omission of disclosures about changes in ICFR after significant events that make material changes likely, such as a business combination or a significant accounting change
- ▶ The effectiveness of disclosure controls and procedures when management concludes that ICFR is ineffective

### *Analysis of current issues*

The SEC staff has expressed concerns that material weaknesses are not being identified timely and that control deficiencies are not being evaluated appropriately before a material misstatement occurs. A registrant's conclusion about the severity of a control deficiency depends on its evaluation of both the likelihood and magnitude of an error occurring without being prevented or detected by its ICFR. That is, in making this evaluation, a registrant does not just focus on whether an error requiring correction occurred or how large such an error was.

The SEC staff has said that registrants sometimes focus their interim or annual disclosures related to a material weakness on the accounting error itself rather than describing whether a control had an ineffective design or failed to operate effectively. In these cases, the SEC staff has asked for additional information on the deficiency, including:

- ▶ The nature and cause of the material weakness (and financial statement error, if applicable)
- ▶ Who identified the material weakness and when it was identified
- ▶ Whether the material weakness affects certain other accounts or processes or is more pervasive
- ▶ The planned actions, costs and timeframe to remedy the material weakness
- ▶ How the registrant compensates for the material weakness to make sure that the financial statements are free from material misstatement
- ▶ The status of any unremediated material weakness that was previously disclosed
- ▶ The effect on disclosure controls and procedures when ICFR is ineffective, given that ICFR constitutes a substantial element of disclosure controls and procedures

The SEC staff also has questioned why a registrant's disclosures under Item 308(c) of Regulation S-K did not identify a material change in ICFR during the most recent quarter if a registrant (1) concludes its ICFR and/or disclosure controls and procedures are ineffective due to a new material weakness or (2) reports the remediation of a previously reported material weakness. The SEC staff may question management's judgment when management attributes a material error to a control deficiency but does not conclude that the deficiency is a material weakness.

When correcting an accounting error, management should carefully reassess the implications for its ICFR and disclosure controls and procedures.

#### **Example SEC staff comment: Material weakness**

We note in your response that you determined there was a control deficiency in your internal control over financial reporting; however, the deficiency did not rise to the level of a material weakness. A control deficiency constitutes a material weakness if there is a reasonable possibility that a material misstatement of the financial statements would not be prevented or detected in a timely manner.

Based on your determination that the disclosure misstatements in your prior SEC filings were material and a result of a control deficiency, we are unable to agree with your conclusion that the related deficiency is not a material weakness. Please explain how you will address and disclose the ineffectiveness of internal control over financial reporting and disclosure controls and procedures for the periods the material weakness existed.

In addition, if there are indicators of control deficiencies in filings, the SEC staff may ask registrants to explain whether those deficiencies were identified by management and, if so, describe their severity, including whether the deficiencies are material weaknesses.

For example, the SEC staff may challenge the effectiveness of ICFR when a registrant corrects an immaterial out-of-period error during the current period without revising prior-period amounts. The SEC staff may question whether the correction of immaterial errors affects current and previous conclusions related to the effectiveness of ICFR and disclosure controls and procedures.

If a registrant determines that ICFR or its disclosure controls and procedures (or both) were effective despite the immaterial error correction, the SEC staff may challenge the basis of these conclusions. In particular, SEC staff often questions the nature of the deficiency that resulted in the error and the likelihood that the deficiency could result in a material misstatement.

#### **Example SEC staff comment: Immaterial error correction and ICFR**

Please explain the extent to which you considered the effect of the identified errors on your internal controls and explain how management's conclusion regarding the effectiveness of disclosure controls and procedures, as well as internal control over financial reporting, is appropriate in light of the errors.

To the extent you determined there were control deficiencies that led to the errors, describe in reasonable detail the deficiencies, how you evaluated the severity of each related deficiency and error in your assessment. Please also include in your analysis a description of the maximum potential amount or total of transactions exposed to each related deficiency and explain how you made that determination.

Items 307 and 308 of Regulation S-K require that management's conclusions about effectiveness explicitly state whether disclosure controls and procedures and ICFR are either "effective" or "ineffective." Generally, the SEC staff challenges registrants that inappropriately express management's conclusions, saying that disclosure controls and procedures are "adequate," "effective, except for" or "effective, to the best of our knowledge."

#### **Example SEC staff comment: Inappropriate management's assessments**

We note your certifying officers concluded your disclosure controls and procedures are effective "subject to the limitations noted above." It is not appropriate to indicate your disclosure controls and procedures are effective subject to certain limitations. You must clearly state whether or not the disclosure controls and procedures are effective. Please amend the Form 10-K to delete the qualification and provide an unqualified conclusion as to the effectiveness of your disclosure controls and procedures.

Disclosure controls and procedures include components of ICFR that (1) relate to the maintenance of records that fairly reflect an issuer's transactions, (2) provide reasonable assurance that the transactions are properly recorded to permit the preparation of financial statements in accordance with GAAP and (3) provide reasonable assurance that unauthorized transactions that could have a material effect on the financial statements have been prevented.

The scope of these procedures would generally include ICFR because they apply to all material information to be included in a report, within and outside the financial statements. The SEC staff has challenged registrants that say they concluded that ICFR was ineffective but disclosure controls and procedures were effective.

#### **Example SEC staff comment: Disclosure controls and procedures and ICFR**

Please explain how you concluded that your disclosure controls and procedures were effective as of December 31, 2016, considering that your internal control over financial reporting was not effective as of this date. Your explanation should be comprehensive and address all of the components of the definition of disclosure controls and procedures.

We refer you to Sections II.D and E of SEC Release 33-8238, in which the Commission recognizes that there is substantial overlap between ICFR and DCPs. For example, DCPs often include those components of ICFR that provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP. Please include in your response an explanation as to how you determined that the material weaknesses in your ICFR were not one of the components of ICFR that is also included in disclosure controls and procedures.

#### ***EY resources***

[2017 SEC annual reports – Form 10-K](#)

[Compendium of significant accounting and reporting issues, 2017 AICPA Conference on Current SEC and PCAOB Developments](#)

[Financial reporting developments, Accounting changes and error corrections](#)

## Materiality

### *Summary of issues noted*

The SEC staff requests that registrants identify and discuss the quantitative and qualitative factors they considered when they assessed the materiality of error corrections. If a registrant concludes that a large error was immaterial, the SEC staff will challenge that conclusion.

### *Analysis of current issues*

SAB Topic 1.M, which appears in ASC 250-10-S99-1, includes a list of possible qualitative and quantitative factors that a registrant might consider when assessing how a reasonable investor might consider the materiality of a financial statement item, including a financial statement error. The factors listed in SAB Topic 1.M are not intended to be exhaustive, and therefore each registrant should consider all qualitative and quantitative factors that may be relevant in its circumstances.

Evaluating whether an item is material requires judgment. Both quantitative and qualitative factors should be considered. Registrants must consider qualitative factors especially when the error is small. It is unusual for a registrant to conclude that a large error is not material based on qualitative factors.

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When assessing materiality, a registrant should analyze both qualitative and quantitative factors.

The SEC staff frequently requests that registrants identify the factors they considered when assessing materiality with respect to current-period and prior-period financial statements when they correct errors relating to a prior period. Management should avoid relying on a “check-the-box” approach that is limited only to the indicators in the staff guidance. Instead, management should develop a qualitative and quantitative analysis that is specific to the registrant’s facts and circumstances and considers each period affected by the error, including quarterly and annual periods. The analysis also should consider the effects of errors on key performance indicators that may be important to investors, even if the indicators are non-GAAP measures.

The SEC staff may question management’s judgment when the error has a large effect on certain key measures.

The SEC staff also challenges materiality assessments for “Little r” restatements. Such a restatement occurs when an error is immaterial to the prior-year financial statements, but correcting the error in the current period would materially misstate the current-period financial statements. As a result, the prior-year financial statements are restated, even though the revision is immaterial to the results for the prior year(s).

In these situations, registrants generally are not required to file an Item 4.02 Form 8-K, *Non-reliance on previously issued financial statements or a Related Audit Report or Completed Interim Review*, or amend prior filings. Instead, they may correct the prior-period financial statements, with appropriate disclosure, in the next periodic report that includes the prior-period financial statements, as outlined in SAB Topic 1.N. The SEC staff may request the registrant’s materiality assessment to evaluate whether the method of correcting the error and related reporting are appropriate.

### **Example SEC staff comment: Materiality**

You indicate that you identified errors in previously issued financial statements associated with a subsidiary that were immaterial to each of the prior reporting periods affected. You also indicate that you have revised the prior-period results in the current filing since the cumulative effect of correcting the errors in 2017 would materially misstate your 2017 financial results. Please tell us:

- ▶ The analysis of how you determined these errors were both quantitatively and qualitatively immaterial to the current period and all previously reported periods (please refer to SAB Topics 1.M and 1.N when preparing your response)
- ▶ The specific nature of these errors, how and why you believe they occurred, and when and how you discovered them
- ▶ Your consideration of the potential effect of these errors on your conclusions on the effectiveness of your internal controls over financial reporting and disclosure controls and procedures

### ***EY resources***

[Financial reporting developments, Accounting changes and error corrections](#)

## Other entity financial statements

### *Summary of issues noted*

SEC regulations require registrants to provide financial information about other entities in certain situations, including when they (1) make a significant acquisition of a business (Rule 3-05 of Regulation S-X), (2) have a significant equity method investee (Rules 3-09 and 4-08(g) of Regulation S-X) or (3) are subject to guarantor reporting requirements (Rule 3-10). The financial statement requirements for each rule are based on whether certain thresholds or criteria are met, and each rule has specific requirements for which financial statements to include in a filing. The SEC staff frequently questions whether registrants have appropriately applied these rules.

### *Analysis of current issues*

#### *Financial statements of an acquired business (Rule 3-05)*

When an acquisition of a significant business has occurred or is probable, Rule 3-05 requires the registrant to file separate, pre-acquisition historical financial statements for the acquired business. The SEC staff frequently requests that the registrant provide its detailed analysis (including the tests of significance) to help the SEC staff determine whether Rule 3-05 was applied appropriately. The SEC staff also questions the completeness of acquiree financial statements included in a filing.

#### **Example SEC staff comment: Significance tests**

It appears that you have not filed historical financial statements pursuant to Rule 3-05 of Regulation S-X. Please submit the analysis you performed to determine that this acquisition was not significant under the investment test, asset test and income test based on the guidance in Rule 3-05 of Regulation S-X, and you were therefore not required to file historical and pro forma financial statements on Form 8-K related to this acquisition, if this is your view.

When a registrant has disclosed letters of intent regarding a potential acquisition in the months before filing a new registration statement, the SEC staff may question whether it is probable that an acquisition exceeding 50% significance will occur, and if so, the SEC staff will ask the registrant to include pro forma information and historical financial statements for the target acquiree in the registration statement.

Furthermore, for purposes of complying with Rule 3-05 in registration statements, tests of significance should be conducted for each consummated and probable acquisition individually and in the aggregate since the last audited balance sheet appearing in the registration statement.

#### **Example SEC staff comment: Disclosures about probable acquisitions**

We note that you have entered into letters of intent regarding potential acquisitions. Please confirm to us that these pending probable acquisitions are not significant and there are no other probable acquisitions that would be significant such that additional historical and pro forma financial statements could be required by Rule 3-05 of Regulation S-X.

#### *Financial statements of equity method investees (Rules 3-09 and 4-08(g))*

When there are indications that a registrant may have significant equity method investees in any of the periods presented but the registrant has not included the separate financial statements or summarized financial information required by Rules 3-09 and 4-08(g), the SEC staff has asked the registrant to provide its analysis, including the detailed significance test computations.

The SEC staff's comments depend on the registrant's facts and circumstances. However, the SEC staff expects strict application of the significance tests. Registrants that inappropriately apply the requirements or fail to timely file investee financial statements may face consequences, such as the loss of Form S-3 eligibility or SEC staff comments challenging whether their disclosure controls and procedures are effective.

#### *Financial statements of guarantors (Rule 3-10)*

The SEC staff often asks registrants about their compliance with the criteria that permit financial reporting relief under Rule 3-10 of Regulation S-X. The staff asks registrants to confirm and disclose that (1) the subsidiary issuers and guarantors are 100% owned rather than "wholly owned," (2) the guarantees are full and unconditional and (3) the guarantees are joint and several.

The SEC staff may also focus on the form and content of condensed consolidating financial information disclosed in the parent company's consolidated financial statements in lieu of separate financial statements for each subsidiary issuer and guarantor of registered debt securities, including whether the individual columns in the consolidating financial information comply with Regulation S-X and are prepared in accordance with US GAAP.

#### **EY resources**

[2017 SEC annual reports – Form 10-K](#)

[Compendium of significant accounting and reporting issues, 2017 AICPA Conference on Current SEC and PCAOB Developments](#)

[Financial reporting developments, Equity method investments and joint ventures](#)

[Technical Line, Tips for complying with the SEC reporting requirements for equity method investees](#)

## Pro forma adjustments

### *Summary of issues noted*

The SEC staff has asked registrants about pro forma financial information disclosed in filings, including registration statements, proxy statements and Forms 8-K. The SEC staff has asked registrants to explain how they have met the requirements of Article 11 of Regulation S-X. The SEC staff also has asked for more transparent disclosure about the calculation of pro forma adjustments.

### *Analysis of current issues*

The objective of pro forma financial information is to provide investors with information about the continuing impact of a particular transaction, such as an acquisition or disposition, that has occurred or is probable after the date of the historical financial statements (or is not fully reflected in the historical financial statements) by showing how it might have affected the registrant's historical financial statements "as if" the transaction had occurred at an earlier time. Article 11 of Regulation S-X describes the circumstances when pro forma information should be presented in SEC filings and the form and content for the presentation.

Pro forma adjustments included in pro forma financial information to provide this "as if" perspective of a transaction must be (1) directly attributable to each specific transaction, (2) factually supportable and (3) expected to have a continuing impact (for the pro forma income statement only). The SEC staff's questions about pro forma adjustments often cite these criteria and ask how pro forma adjustments comply with them.

### *Directly attributable*

Pro forma adjustments should be directly attributable to the transaction reflected in the pro forma financial information. Pro forma financial information should exclude adjustments that reflect how the acquirer might have changed the acquiree's management practices and operating decisions had the acquirer had control over the acquiree during the period of the pro forma presentation.

The SEC staff has questioned adjustments that do not appear to be directly attributable to the transaction reflected in the pro forma financial information. For example, in pro forma information giving effect to a significant acquisition, a restructuring charge recognized in the target's historical financial statements would generally not be considered directly related to the business combination and should not be eliminated from the pro forma financial information. Furthermore, any integration restructuring activities and anticipated cost savings that the acquirer intends to implement after the acquisition would also generally not be considered directly related to the business combination and their effects should not be included in the pro forma financial information.

### **Example SEC staff comment: Pro forma adjustments**

We note that you have included a pro forma adjustment to eliminate compensation to the company's chief executive officer because he or she will perform limited duties under a consulting agreement subsequent to this offering and acquisition. Since we assume that the compensation historically paid was commensurate with the duties he or she performed, please revise to eliminate this adjustment.

Registrants should clearly disclose the nature of pro forma adjustments and how they are calculated.

#### *Factually supportable*

Pro forma adjustments should be factually supportable. The SEC staff has indicated that an adjustment generally would be considered factually supportable if there is reliable documented evidence, such as an executed contract or completed transaction. For example, the SEC staff has challenged registrants when they include in their adjustments the effects of a new compensation arrangement that they expect to implement following a business combination if an agreement for such compensation was not executed in conjunction with the business acquisition negotiations.

The SEC staff also has indicated that the effects of some events and transactions are too uncertain to be considered factually supportable. For example, a company should not eliminate compensation expense on a pro forma basis for employees terminated following a business combination because the effects on revenues and operations from having fewer employees would be too uncertain.

#### *Continuing impact*

Pro forma income statement adjustments must have a continuing impact on the registrant or remove from the historical financial statements transaction-related costs or other items that are not expected to have a continuing impact. The SEC staff has asked registrants to explain how an adjustment has a continuing impact.

The SEC staff has historically used a 12-month rule of thumb to evaluate the continuing impact criterion. However, certain items that affect the pro forma income statement for a period of less than 12 months may still be considered to have a continuing impact. The evaluation will depend on the registrant's facts and circumstances. For example, an adjustment for interest expense on a bridge loan that may be incurred for a period of less than 12 months might be considered to have a continuing impact because such loans are typically replaced with permanent financing shortly after an acquisition closes.

#### **Example SEC staff comment: Pro forma adjustments**

We note your disclosure that you have included an adjustment to the pro forma statement of operations to recognize a \$5 million 3% call premium for the repayment of debt. Please tell us how you determined that this expense is a recurring item and revise your disclosures accordingly. Please refer to Articles 11-02(b)(5) and 11-02(b)(6) of Regulation S-X for guidance.

#### *Transparency of pro forma adjustments*

In addition to meeting the criteria in Article 11 of Regulation S-X, pro forma adjustments should be clearly presented. The following disclosures should be included in the notes to the pro forma financial information:

- ▶ The nature of pro forma adjustments
- ▶ How pro forma adjustments are calculated
- ▶ The assumptions used to determine such amounts

For example, if two partially offsetting pro forma adjustments are presented in the aggregate to adjust deferred tax liabilities in the pro forma balance sheet, the notes to the pro forma financial information should explain the two gross adjustments in the net adjustment presented on the face of the pro forma financial information. The SEC staff often asks for clarification or additional disclosure when it's unclear how pro forma adjustments were calculated or when the amount of the total or net adjustment does not agree with the underlying gross pro forma adjustments explained in the notes.

**Example SEC staff comment: Pro forma adjustments**

Please expand your disclosure to provide a more detailed description of all of the pro forma adjustments reflected. Your revised disclosure should include a discussion of the methodologies used by the company to determine fair value as well as a listing of any material assets or liabilities currently shown net in the footnote (i.e., above-market lease intangibles and lease origination costs reflected as "lease intangible assets").

***EY resources***

[Pro forma financial information: A guide for applying Article 11 of Regulation S-X](#)

## Rule 4-08(e) disclosures

### *Summary of issues noted*

The SEC staff has asked registrants about third-party restrictions that appear to limit their ability to (1) pay dividends to shareholders or (2) transfer net assets from subsidiaries. If such restrictions exist, the SEC staff asks registrants to disclose them as required by Rule 4-08(e) of Regulation S-X. The SEC staff has also asked registrants about how they considered the requirements under Rule 5-04 of Regulation S-X to present condensed financial information on an unconsolidated basis (i.e., parent company financial statements).

### *Analysis of current issues*

The SEC staff often issues comments about Rule 4-08(e) disclosures to registrants in the insurance and midstream oil and gas industries because of their legal structures, but the disclosure requirement applies to all registrants.

The SEC staff may use a registrant's debt agreements filed as exhibits, risk factor disclosures and financial statement disclosures about debt as the basis for inquiring about compliance with the requirements of Rule 4-08(e).

For example, a registrant's risk factor disclosure may indicate that a subsidiary's debt agreements limit the subsidiary's ability to pay distributions to the registrant. The SEC staff has asked such registrants to quantify in their response letter the amount of the subsidiary's restricted net assets, as defined in Rule 4-08(e)(3) of Regulation S-X, as of the end of the most recently completed fiscal year and explain how this amount was computed.

The SEC staff also has asked registrants about their compliance with Rules 5-04(c) and 12-04 of Regulation S-X. Rule 5-04(c) requires registrants to include parent-only condensed financial information on Schedule I, *Condensed financial information of registrant*, using the form and including the content required by Rule 12-04 when restricted net assets of only the registrant's consolidated subsidiaries exceed 25% of the registrant's consolidated net assets. This schedule shows investors the amount of net assets, operations and cash flows at the parent level on a standalone basis with all subsidiaries reflected on an unconsolidated basis (i.e., under the equity method).

### **Example SEC staff comment: Rule 4-08(e) disclosures and parent-only financial information**

You disclose that the restricted payments covenant in the indenture governing your subsidiaries' notes as well as restrictions in your credit facility generally limit your ability to pay dividends. Please discuss any restrictions on your ability to declare dividends and the impact on your liquidity, financial condition and results of operations based on these restrictions. Please provide, if necessary, the disclosures required by Rule 4-08(e) of Regulation S-X. Please also tell us what consideration you gave to the need for parent-only financial statements under Rules 5-04 and 12-04 of Regulation S-X.

### **EY resources**

[2017 SEC annual reports – Form 10-K](#)

## Other SEC reporting issues

### *Summary of issues noted*

The SEC staff has questioned how a registrant complies with the various disclosure requirements of Regulation S-K or other SEC rules and has requested additional disclosures, if material.

### *Analysis of current issues*

The following is a brief overview of SEC disclosure areas where the staff continues to issue comments requesting compliance.

#### *Business disclosures*

Item 101 of Regulation S-K requires disclosure about the registrant's business, including a description of its products or services and geographic areas. Although the nature of SEC staff comments varies significantly in this area, depending on the registrant's facts and circumstances, the SEC staff typically has commented on the required disclosures about backlog, customer concentration, material supply/collaboration agreements and patents. The SEC staff has used a registrant's publicly available information (e.g., quarterly earnings calls, investor presentations) to challenge the completeness and accuracy of the disclosures provided.

#### *Selected quarterly financial data*

When disclosing quarterly financial data required by Item 302 of Regulation S-K, the registrant must explain the effect of any disposals of segments of a business, any unusual or infrequently occurring items recognized in each quarter (e.g., data security incidents, restructurings, acquisitions) and the aggregate effect and nature of year-end or other adjustments that are material to the results of the fourth quarter (e.g., changes in pension plan assumptions). The SEC staff issues comments when such items are not transparently disclosed as a note to the table of selected quarterly financial data, even if they are addressed elsewhere in the filing (e.g., MD&A).

#### **Example SEC staff comment: Selected quarterly financial data**

We note from your disclosure of selected quarterly financial data that the net loss recorded in the third quarter of 2017 was significantly different from the net incomes recorded in the other 2017 quarterly periods. Please revise to include disclosure of your restructuring activities, acquisition costs, legal settlements or impairment charges that materially affected the results of operations in your quarterly periods for 2017. See guidance in Item 302(a)(3) of Regulation S-K.

When preparing their tabular disclosure of selected quarterly financial data, registrants should keep in mind the definition of gross profit in Item 302(a)(1) of Regulation S-K. Expenses associated directly with or allocated to products and services are expected to include depreciation of property and amortization of intangibles deployed in the production and delivery of the products or performance of the services. Accordingly, the SEC staff may question a registrant's basis for presenting all of its depreciation and amortization outside of gross profit in the table of selected quarterly financial data or may request that the registrant change the composition of its quarterly gross profit altogether.

Registrants are expected to exercise particular diligence and judgment in preparing disclosures about their transactions with related parties.

#### *Risk factors*

Item 503(c) of Regulation S-K requires a registrant to disclose the significant risks it faces and how it is affected by each of them. Risk factors should be specific to the registrant's facts and circumstances and should not be general risks that could apply to any registrant. The SEC staff has questioned risk factor disclosures that could apply to any public company as well as limitations that some registrants include in their risk factor disclosures that do not comply with item 503(c) of Regulation S-K. The SEC staff also has questioned the completeness of a registrant's risk factor disclosures based on information included elsewhere in the document or in other public information (i.e., an earnings call).

With the increase in the frequency and severity of cyberattacks and data breaches, cybersecurity continues to be an area of focus. The SEC has issued an interpretive release to help companies prepare disclosures about cybersecurity risks and incidents. The release includes a framework for registrants to consider when evaluating whether to disclose information about risks and incidents involving cybersecurity. The framework is similar to the one previously established by the SEC staff in CF Disclosure Guidance: Topic No. 2. The release also reminds registrants to consider cyber matters in the context of various policies such as those for insider trading and selective disclosure (Regulation FD).

#### *Related-party transactions*

The SEC staff may request that registrants clarify or expand their disclosures about related-party transactions as required by Item 404(a) of Regulation S-K. Item 404(a) requires a registrant to describe related-party transactions (both actual and proposed) exceeding \$120,000 since the beginning of its last fiscal year and in which any related party had or will have a direct or indirect material interest. The SEC staff expects the description of a particular transaction to summarize the nature of the transaction in quantitative and qualitative terms and include any material additional information.

The SEC staff often questions the completeness of disclosures provided under Item 404(a) and inconsistencies with the notes to registrants' annual and interim financial statements, disclosures in the business and risk factors sections, and any new agreements filed as exhibits. Preparing complete related-party disclosures is often challenging because registrants and their advisers have to consider whether information regarding a related-party transaction or the related person in the context of the transaction is material to investors in light of the circumstances of the particular transaction.

For example, the SEC staff recently has questioned registrants that fail to disclose indemnification provisions included in agreements with their executive officers.

Registrants sometimes overlook the fact that the requirements for disclosures about notes payable from officers to a registrant are much more prescriptive and granular than those for other related-party transactions. In those cases, the SEC staff has reminded registrants about the requirements of Item 404(a)(5) to disclose not only the principal balance outstanding as of the end of the reporting period and the interest rate but also the largest aggregate amount of principal outstanding during the period and the amount of principal repaid during the period.

The SEC staff requires that registrants comply with Rule 4-08(k) of Regulation S-K and identify all of their related-party transactions on the face of the balance sheet and statements of income and cash flows when their related-party disclosures are material.

*State sponsors of terrorism*

The SEC staff may comment on disclosures about liquidity, risk factors and results of operations for registrants with foreign operations in countries that have been identified by the US Department of State as state sponsors of terrorism, including Syria, Iran, North Korea and Sudan. The SEC staff will search a registrant's publicly available information (e.g., websites, news articles) for connections to the restricted countries, including comments related to unaffiliated retail locations where a registrant's branded product is sold. For further discussion, please refer to *Appendix C: Foreign private issuers*.

**EY resources**

[2017 SEC annual reports – Form 10-K](#)

[Pro forma financial information – A guide for applying Article 11 of Regulation S-X](#)

[New SEC Chairman Jay Clayton outlines views in policy speech](#)

[SEC Reporting Update, SEC issues guidance on cybersecurity](#)

# Financial statement presentation

## Income statement presentation

### *Summary of issues noted*

The SEC staff continues to ask registrants to provide information supporting their conclusions on the appropriate presentation of revenue and cost of sales in the income statement. Specifically, the SEC staff focuses on the income statement presentation guidance in Rules 5-03(b)(1) and (2) of Regulation S-X.

### *Analysis of current issues*

Many registrants derive revenues from the sale of different product categories or the sale of both products and services. In such cases, presentation of revenues by category may provide meaningful information to the users of the financial statements, particularly if the gross margins of the various categories of sales transactions are disparate. Rule 5-03(b)(1) of Regulation S-X requires the following items to be separately stated on the face of the income statement, unless the amount is less than 10% of total revenue:

- ▶ Net sales of tangible products (gross sales less discounts, returns and allowances)
- ▶ Operating revenue of public utilities or others
- ▶ Rental income
- ▶ Revenue from services
- ▶ Other revenues

Rule 5-03(b)(2) of Regulation S-X requires that costs and expenses applicable to sales and revenues be presented on the face of the income statement in the same categories as the corresponding revenue.

When other disclosures in a registrant's filings (e.g., MD&A discussion) or public materials (e.g., an earnings release) refer to revenue being derived from various sources, the SEC staff asks registrants to provide their analyses and other information (including quantitative data by revenue source) that was used to conclude on the income statement presentation of revenue and cost of sales. Registrants should continuously monitor the relative proportion of revenue earned from each source to make sure they are properly presenting revenue and cost of sales attributable to each significant category.

### **Example SEC staff comment: Rule 5-03(b)**

Please separately present sales and cost of sales for products and services on the face of your statements of operations pursuant to Rules 5-03(b)(1) and (2) of Regulation S-X.

Furthermore, under ASC 606, registrants are required to provide a note disaggregating revenue recognized from contracts with customers into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors. This disaggregation should be performed using the criteria outlined in ASC 606-10-50-89 through 91 and is in addition to the disaggregated revenue presentation on the face of the income statement required by Rule 5-03(b) of Regulation S-X. Refer to the *Revenue recognition – Disaggregated revenue disclosures* section for further information on SEC staff comments about this disclosure requirement.

The SEC staff continues to challenge the income statement presentation of revenue and related costs attributable to various products and services.

# Accounts receivable

## Allowance for doubtful accounts

### *Summary of issues noted*

The SEC staff asks registrants to provide a robust description of their accounting policies and methods used to estimate the allowance for doubtful accounts. The staff also asks registrants to explain both significant changes in the allowance from the prior period and changes that appear unusual in relation to other financial statement accounts. Further, the staff asks registrants for additional information on the credit quality of accounts receivable. In some cases, the staff asks questions about portfolio segments or customers that may be material to a registrant's operations.

### *Analysis of current issues*

ASC 310 provides the disclosure requirements for accounts receivable. Registrants with sales that result in accounts receivable should have accounting policies and methods to estimate the allowance for doubtful accounts. They also should have policies for tracking delinquencies, determining when receivables become impaired and writing off uncollectible receivables. The SEC staff requests disclosure about how a registrant assesses collectability of receivables and determines its allowance for doubtful accounts, including the significant assumptions used and any uncertainty relative to those assumptions.

The staff asks for more details on the methods and assumptions used to determine the allowance.

### **Example SEC staff comment: Allowance for doubtful accounts**

Given the nature and impact of the estimates and assumptions surrounding your assessment of the collectability of your accounts receivable, expand your disclosures to address the material implications of uncertainties associated with the methods, assumptions and estimates underlying your accounting for accounts receivable and the related allowance for doubtful accounts.

The expanded disclosure should also address, to the extent material, factors such as how you arrived at your estimates, how accurate the estimates have been in the past, how much the estimates have changed in the past, and whether the estimates are reasonably likely to change in the future.

When conditions cause significant or unusual changes in accounts receivable or in the allowance for doubtful accounts, the SEC staff asks registrants to disclose the factors that led to the changes. The staff asks registrants to disclose whether any specific customers or portfolio segments disproportionately drove the changes. The staff also questions whether the changes indicate trends that may have a material effect on the registrant's financial condition and/or results of operations, which would have to be disclosed in MD&A.

# Business combinations

## Business combinations disclosure

The SEC staff has asked whether registrants have properly characterized changes to initial amounts recognized as measurement period adjustments rather than error corrections.

### *Summary of issues noted*

The SEC staff has asked registrants to enhance or explain their disclosures about business combinations by:

- ▶ Presenting all of the disclosures required by ASC 805, including the pro forma information required by ASC 805-10-50-2(h)
- ▶ Providing supplemental information related to the appropriateness of measurement period adjustments
- ▶ Providing the SEC staff with information and expanding disclosures about contingent consideration arrangements
- ▶ Providing the SEC staff with information about how they identified and determined the fair value of acquired intangible assets, especially when goodwill is a substantial portion of the consideration transferred
- ▶ Explaining how they evaluated whether the acquired set of assets and activities constituted a business or an asset

### *Analysis of current issues*

#### *General disclosures*

The disclosures in ASC 805 are intended to help financial statement users evaluate:

- ▶ The nature and financial effect of business combinations that occur during the current reporting period or after the balance sheet date but before the financial statements are issued
- ▶ The financial effects of adjustments recognized in the current reporting period that relate to a business combination that occurred in the current or previous reporting periods

The SEC staff has questioned whether registrants' disclosures about business combinations are sufficient and requested that registrants expand their disclosures to provide material information required by ASC 805.

#### **Example SEC staff comment: General disclosures**

Please address the following:

- ▶ Provide a table in the footnotes for the fair value of the major classes of assets acquired and liabilities assumed. As part of this presentation, please separately present each major class of property, plant and equipment and identifiable intangible assets acquired. Refer to ASC 805-20-50-1.
- ▶ Please tell us where you disclosed the primary reasons for the acquisition as required by ASC 805-10-50-2(d). If this disclosure was not provided, please provide it in your upcoming filing.

When goodwill resulting from a business combination represents a significant portion of the consideration transferred, the SEC staff has asked registrants to revise their disclosures to provide more specifics in their qualitative descriptions of the factors that make up the amount of goodwill recognized (e.g., the specific synergies expected from the business combination) as required by ASC 805-30-50-1.

**Example SEC staff comment: Disclosures relating to goodwill recognized**

Given the significant amount of purchase consideration allocated to goodwill, please describe the qualitative factors that make up goodwill, such as expected synergies from the combining operations, intangible assets that do not qualify for separate recognition or other factors. Refer to the guidance outlined in ASC 805-30-50-1.

ASC 805-10-50-2(h) requires pro forma disclosures assuming the acquisition occurred as of the beginning of the comparable prior annual reporting period. When pro forma disclosures are not provided, the SEC staff has asked the registrant to explain why it is impracticable for the registrant to prepare the disclosures or to explain why the disclosure is not material. It is important to note that the evaluation of materiality for this purpose is separate and distinct from the significance test performed for the purposes of presenting Article 11 pro forma financial information.

**Example SEC staff comment: Pro forma disclosures**

Please tell us your consideration of disclosing the following information to enable users of your financial statements to evaluate the nature and financial effect of the acquisition in accordance with ASC 805-10-50-2(h):

- ▶ The amounts of revenue and earnings of the acquiree since the acquisition date included in the consolidated income statement for the reporting period
- ▶ The revenue and earnings of the combined entity for the current reporting period as though the acquisition date for the business combination that occurred during the year had been as of the beginning of the annual reporting period
- ▶ The revenue and earnings of the combined entity as though the acquisition that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period

*Measurement period adjustments*

The SEC staff has asked registrants to provide supplemental information about whether adjustments to provisional amounts recognized for assets acquired or liabilities assumed in a business combination qualify as measurement period adjustments, including whether registrants have properly characterized changes to the provisional amounts recognized in the acquisition as measurement period adjustments rather than error corrections.

The measurement period, which cannot exceed one year, ends when a registrant obtains the additional information that it was seeking about facts and circumstances that existed as of the acquisition date or when it concludes that such information is not obtainable. The SEC staff also asks registrants to disclose that the initial measurement of provisional items is incomplete.

### **Example SEC staff comment: Measurement period adjustment**

We note your disclosures regarding the acquisition of a business. Please more fully address the following:

- ▶ You indicate that additional measurement period adjustments to indefinite and finite-lived assets, customer relationships and license agreements were the result of changes in assumptions used for valuation purposes such as projected growth rates, profitability and discount rates. More fully explain your revised assumptions, the reasons for the revisions, and the reasons for the significant differences in the allocations disclosed here relative to amounts disclosed in your Form 10-K.
- ▶ Explain the nature of any additional information you are awaiting to finalize the purchase price allocation.

#### *Contingent consideration arrangements*

The SEC staff has asked registrants to provide more robust descriptions of any contingent consideration arrangements and the basis for estimating the amount of the future payments. The SEC staff also has asked registrants to explain how they account for and determine the fair value of contingent payments to former owners both as of the acquisition date and in subsequent periods, including whether payments represent compensation or consideration. In addition, the SEC staff may request that registrants enhance their disclosures based on its review.

#### *Identification and valuation of acquired intangible assets*

The SEC staff has challenged whether additional intangible assets should have been recognized in a business combination and whether the valuation of an acquired intangible asset is appropriate. This is often the case when registrants have allocated a significant portion of the purchase price to goodwill. For further discussion, please refer to the *Intangible assets* section of this publication.

#### *Determination of business or asset acquisition*

When a registrant's disclosure about the acquired assets and activities is unclear, the SEC staff has asked registrants to explain how they evaluated whether the acquired set constitutes a business or an asset. The SEC staff has said that it may question a registrant's conclusion when the difference in accounting could be material, such as in transactions involving significant premiums, transaction costs or contingent consideration.

#### **EY resources**

[Financial reporting developments, Business combinations](#)

# Consolidation

## Variable interest entity consolidation, noncontrolling interests and disclosures

The SEC staff expects registrants to avoid boilerplate disclosures about their consolidation conclusions.

### *Summary of issues noted*

The SEC staff has asked registrants to:

- ▶ Explain how they determined whether an entity is a variable interest entity (VIE), including how they evaluated details of the arrangement and the registrants' involvement with the entity
- ▶ Explain how they determined whether they were or were not the primary beneficiary of a VIE
- ▶ Provide additional details related to their noncontrolling interests, including their computation of ownership interests and net income or loss attributable to their noncontrolling interests
- ▶ Provide enhanced disclosures about their consolidation accounting policy and how they determined whether they have controlling financial interests

### *Analysis of current issues*

#### *Primary beneficiary determination*

The SEC staff has asked registrants to provide supplemental information about their primary beneficiary determination, focusing particularly on the decisions about the activities that most significantly impact the VIE's economic performance.

#### **Example SEC staff comment: Primary beneficiary determination**

We note from your disclosure that Entity A is determined to be a VIE, which you consolidate as a result of being the primary beneficiary. Please provide us with your analysis of how you determined that you are the primary beneficiary. Please cite the applicable guidance in your response.

#### *Income and losses attributable to noncontrolling interests*

The SEC staff has asked registrants to explain how they determine income and losses attributable to noncontrolling interests, including their valuation methodology. In certain cases, the SEC staff has requested example calculations to support their attribution.

#### **Example SEC staff comment: Income and losses attributable to noncontrolling interests**

Provide us with further detail to support the allocation of net income (loss) attributable to the noncontrolling interests.

#### *Disclosures*

The SEC staff continues to remind registrants that ASC 810-10-50 requires disclosure of qualitative and quantitative information about involvement with a VIE, including, but not limited to, the nature, purpose, size and activities of the VIE. ASC 810-10-50-2AA(a) requires registrants to disclose the significant judgments and assumptions they made in determining whether they must consolidate a VIE or disclose information about their involvement with a VIE. ASC 810-10-50-2AA(d) also requires registrants to disclose how their involvement with a VIE affects their financial position, financial performance and cash flows.

### **Example SEC staff comment: Disclosures**

It appears based on your disclosure that most of your operations stem from the consolidation of your VIE, Entity A. As such, please expand your disclosure to include the disclosures required by ASC 810-10-50-2AA(b) and (c). Also, in accordance with ASC 810-10-50-2AA(d), disclose how your involvement with your VIEs affects your cash flows.

The SEC staff expects registrants to avoid making boilerplate disclosures of the facts and circumstances they evaluated to determine the primary beneficiary and reach their consolidation conclusions. For example, the SEC staff has cautioned registrants that merely listing the contractual arrangements between a registrant and the VIE does not provide sufficient insight into the judgments the registrant made in evaluating whether to consolidate the VIE.

### ***EY resources***

*Financial reporting developments, Consolidation – Determination of a controlling financial interest and accounting for changes in ownership interests*

# Contingencies

## Accounting for and disclosure of loss contingencies

### *Summary of issues noted*

Over the past few years, we have seen loss contingencies reemerge as a frequent area of comment. In its comments on registrants' compliance with loss contingency disclosure requirements, the SEC staff focuses on disclosures about reasonably possible losses and the clarity and timeliness of loss contingency disclosures.

### *Analysis of current issues*

The SEC staff questions a registrant's failure to make required note disclosures when losses are considered reasonably possible or to disclose the range of reasonably possible losses, including when there is a reasonable possibility of a loss in excess of the amount accrued. The SEC staff seeks to verify that a registrant has considered and disclosed an estimate of the amount or range of reasonably possible losses or, if applicable, made a specific disclosure that the amount of loss cannot be estimated.

The SEC staff generally has not objected when registrants make either of the following disclosures, as applicable, about reasonably possible losses to comply with ASC 450:

- ▶ The amount or range of reasonably possible losses on an aggregate basis<sup>1</sup>
- ▶ The amount or range of reasonably possible losses in certain cases and a statement that the registrant cannot estimate an amount for other cases

The SEC staff has questioned how a registrant has determined that an estimate of a reasonably possible loss or range of loss cannot be made in a reporting period. If a registrant cannot make an estimate, the SEC staff expects the registrant to undertake sufficient procedures to support its conclusion and may request additional information about the process.

If a registrant says an estimate cannot be made, the SEC staff looks for information (such as the registrant's history with similar legal matters and the age of the litigation) that may indicate otherwise. The SEC staff challenges disclosures that imply a need for precision in estimating the loss or range of loss because US GAAP does not require a level of "certainty" or "confidence" for such an estimate.

The SEC staff also has challenged the use of limited time periods to develop a loss estimate when losses are reasonably expected to continue beyond the timeframe used to develop the estimate. An example would be a contingency measured using expected payments over a five-year period if losses are expected to continue beyond that period.

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<sup>1</sup> While it is acceptable to aggregate the amount or range of all reasonably possible losses, the SEC staff has objected to the aggregation of losses in all categories (i.e., it is not acceptable to disclose one estimate combining probable, reasonably possible and remote loss contingencies).

### **Example SEC staff comment: Accounting for and disclosure of loss contingencies**

We note that you disclose several legal matters and, in some instances, you indicate that you intend to vigorously defend the action and you have not reserved for any potential future payments in addition to the amounts accrued. In accordance with ASC 450-20-50, please revise future filings to clearly disclose the following information for your loss contingencies in aggregate or individually: (1) the amount or range of reasonably possible losses in addition to the amounts accrued or (2) a statement that the reasonably possible losses cannot be estimated or are not material to your financial statements.

The SEC staff requests that a registrant's disclosures use terms that are consistent with the language in ASC 450 when discussing the likelihood of occurrence (i.e., probable, reasonably possible or remote) and the estimated reasonably possible loss (i.e., additional loss, range of loss, an estimate cannot be made or the estimated additional loss or range of loss is not material).

The SEC staff also expects management to evaluate its loss contingency disclosures (or lack thereof) in each reporting period. The SEC staff expects those disclosures to evolve to include more quantitative information as the loss contingency progresses. The SEC staff sometimes issues comments on the same matter in subsequent annual and quarterly periods.

Further, the SEC staff may challenge the adequacy of historical disclosures when loss contingencies have been settled. In particular, the SEC staff reviews prior-period disclosures and inquires whether disclosures or accruals were sufficient in the prior periods based upon the development of the matter.

#### ***Presentation of insurance recoveries***

The SEC staff has questioned the presentation of any insurance recoveries on the balance sheet (i.e., whether they are presented as assets versus as reductions of the related loss contingencies) as well as their disclosure. ASC 210-20, *Balance Sheet – Offsetting*, provides guidance on how to determine whether assets and liabilities can be offset and presented on a net basis. We believe it would be rare for all of the criteria in ASC 210-20 to be met for insurance recoveries related to loss contingencies.

# Debt

## Modifications, exchanges, extinguishments or troubled debt restructurings

The SEC staff may ask for supplemental information to better understand how a registrant applied the relevant accounting guidance to such transactions.

### *Summary of issues noted*

Registrants continually evaluate their liquidity and capital structure and often refinance existing debt in response to changes in the economic environment (e.g., declining interest rates, improved entity-specific credit). They may amend the terms of existing debt and/or exchange existing debt for new debt. They also may partially prepay amounts outstanding or borrow more, possibly as a result of exercising rights provided for in the existing agreement. The accounting for such transactions varies significantly, depending on whether a transaction is considered a debt modification or extinguishment, or a troubled debt restructuring. The SEC staff may ask for supplemental information to better understand how the registrant applied the relevant accounting guidance to these transactions.

### *Analysis of current issues*

Registrants should consider the guidance in ASC 470-50 and ASC 470-60 when evaluating debt modifications and should be prepared to provide a thorough accounting analysis for the transaction in response to questions from the SEC staff.

#### **Example SEC staff comment: Debt modification or exchange**

We noted that you refinanced your existing 2018 term loan with another term loan with an aggregate principal amount of \$500 million maturing on 31 December 2020 and accounted for the transaction as a modification. Please refer to ASC 470-50-40-10 and tell us how you determined that these instruments were not substantially different.

In the past, the SEC staff has requested registrants to explain:

- ▶ The calculation of the gain or loss recognized in a debt modification or exchange transaction, including the amount of costs or fees that were capitalized or expensed and the amount included in the gain or loss
- ▶ How a modification or exchange of a cash convertible instrument accounted for under ASC 470-20 was considered in accordance with ASC 470-50, and the determination of the fair value of the modified instrument, gain or loss and related journal entries
- ▶ Whether the recognition of a gain or loss is appropriate for an extinguishment when the transaction is between related parties
- ▶ How a remarketing was considered under ASC 470-50, and the determination of whether a third-party intermediary was acting as an agent or a principal in the transaction

#### **EY resources**

[Financial reporting developments, Issuer's accounting for debt and equity financings](#)

# Earnings per share

## Allocation of income and losses under the two-class method

The SEC staff has asked registrants how income and losses are allocated to participating securities under the two-class method.

### *Summary of issues noted*

The SEC staff has asked registrants for additional information about how they allocate income and losses to each class of common stock and participating securities under the two-class method used to compute earnings per share.

### *Analysis of current issues*

Companies sometimes issue securities that participate in distributions with common stock based on a predetermined formula. These securities are referred to as participating securities. ASC 260 requires entities that issue participating securities or that have multiple classes of common stock to apply the two-class method to compute basic and diluted EPS.

A common example of a participating security is preferred stock that receives dividends based on the dividends paid on common stock. Under the two-class method, EPS is calculated for each class of common stock and participating security considering both dividends declared (or accumulated) and the contractual participation rights in undistributed earnings as if all such earnings had been distributed during the period.

Under the two-class method, the income allocated to a participating security is based only on objectively determinable, nondiscretionary participation rights. Other terms that are subjective or in management's control (e.g., management's determination of an extraordinary dividend) would not be considered. Additionally, losses are allocated to a participating security based on its contractual rights and obligations. However, it is unusual for securities other than common stock to have terms that require a company to allocate its losses to those securities.

The SEC staff has asked registrants to clarify and provide additional disclosure about the basis for allocating income and losses to each class of common stock and participating security and how they determined the effect on earnings per share under the two-class method.

### **Example SEC staff comment: Allocation of income and losses under the two-class method**

Please tell us, and revise to disclose, your basis (including your consideration of ASC 260-10-45-60 to 60B) for allocating net income and losses and determining earnings per unit for each participating security. Please also specifically address the impact on earnings per unit.

### *EY resources*

[Financial reporting developments, \*Earnings per share\*](#)

[Financial reporting developments, \*Share-based payment\*](#)

# Fair value measurements

## Disclosures of valuation techniques and inputs

### *Summary of issues noted*

Fair value measurement continues to be a frequent area of scrutiny by the SEC staff. In its comments on registrants' compliance with fair value measurement disclosure requirements, the SEC staff focuses on disclosures about valuation techniques and inputs used in fair value measurements.

### *Analysis of current issues*

The SEC staff asks registrants to provide more robust disclosures about the valuation techniques and inputs they use in determining fair value, including valuation techniques and inputs used by third parties. The staff's questions continue to be granular, frequently focusing on specific inputs to a fair value measurement. For example, the staff may inquire about the basis for the valuation methodology applied and the basis for inputs used in the valuation, such as discount rates, selected valuation multiples, cash flow forecasts and discounts/premiums applied. Further, the staff may inquire about the "weighting" assigned to multiple value indications when registrants use more than one valuation technique (e.g., internal model valuations and pricing indications from independent sources). In other instances, the SEC staff asks registrants to explain the basis for the valuation methods used to allocate the purchase price among acquired tangible and intangible assets in a business combination.

#### **Example SEC staff comment: Valuation methodology and inputs**

Tell us in reasonable detail how you determined the fair value of your reporting unit. Please include the specific methods utilized. Tell us the material assumptions used under each method utilized. Examples might include how cash flows were estimated, which discount rate was used and which principal market and market participants were selected. Please make sure your response addresses how you determined that each of the assumptions used was appropriate.

#### **Example SEC staff comment: Multiple valuation techniques**

Please address the following comments related to your interim goodwill impairment test. You indicate that you used a discounted cash flow analysis method (income approach) along with the market multiples method (market approach), which you used for additional validation of your fair value calculations. Please tell us whether you weighted both the income and market approaches in developing the fair value of your reporting unit. If so, tell us the relative weighting you used for each approach and how you determined such weighting was appropriate. Tell us whether there would have been any change in your impairment analysis had you solely used a market or income approach or had you changed the relative weighting.

The SEC staff continues to ask registrants to describe the procedures they perform to validate the fair value measurements obtained from third-party pricing services, including how they concluded bid quotes were a reliable indicator of fair value.

#### **Example SEC staff comment: Third-party pricing information**

We note you disclose that you determine the fair value of your investment securities based upon fair value estimates obtained from multiple third-party pricing services and dealers. Also, we note your disclosure that third-party pricing sources use various valuation approaches, including market and income approaches, and you disclose various inputs but no specific techniques. Please describe the specific valuation techniques used, and the inputs applicable to such valuation techniques, to determine the fair value of securities categorized within Level 2.

#### **Example SEC staff comment: Third-party pricing information**

Please tell us how you concluded bid quotations were a reliable indicator of fair value, considering that the quotations don't necessarily represent actual transactions, the market illiquidity of your shares, the large number of shares issued in the exchange, the value at which you issued shares for cash during the same period and other factors.

The SEC staff also comments on disclosures about fair value measurements categorized in Level 3 of the fair value hierarchy. These comments generally focus on a registrant's failure to provide required disclosures about valuation techniques and inputs and quantitative information about the significant unobservable inputs used in the fair value measurement. For example, the staff may ask why a registrant does not disclose the sensitivity of the Level 3 measurement to changes in significant unobservable inputs or may request that the registrant provide the range of unobservable inputs used to value Level 3 measurements.

#### **Example SEC staff comment: Level 3 disclosures**

Please revise future filings to provide all of the disclosures required by ASC 805-30-50-1(c) when a business combination that includes contingent consideration occurs in the reporting period. Revise future filings to reconcile the opening and closing balance and disclose the valuation techniques and the quantitative information about the significant unobservable inputs underlying the Level 3 fair value measurements for the contingent consideration.

#### ***EY resources***

[Financial reporting developments, Fair value measurement](#)

# Financial instruments

## Redeemable equity instruments and redeemable noncontrolling interests

The SEC staff may ask registrants how they account for redeemable equity instruments (including noncontrolling interests).

### *Summary of issues noted*

The SEC staff has asked registrants how they account for redeemable equity instruments and redeemable noncontrolling interests (NCI).

### *Analysis of current issues*

Redeemable equity instruments (e.g., preferred shares) may be classified as liabilities under ASC 480 if the registrant is unconditionally obligated to redeem them. Otherwise, they often are classified in temporary equity or the “mezzanine” section of the balance sheet and measured at, or accreted to, their redemption values. The accounting for these instruments is complex and based partly on the nature of the redemption feature.

Holders (or issuers) of NCI may have many reasons to contractually agree to sell (or buy) the NCI at some point in the future through a contractual redemption feature. When accounting for such a redemption feature, registrants need to consider the feature’s form (i.e., whether it is embedded or freestanding), its nature (i.e., option-like or forward-like) and its pricing (i.e., fixed, variable or fair value), along with the guidance that applies to each of the variables.

The primary guidance to be considered for classification of and accounting for these instruments is in ASC 480, ASC 810, ASC 815 and the SEC’s guidance in ASC 480-10-S99-1, ASC 480-10-S99-2 and ASC 480-10-S99-3A.

The SEC staff has asked registrants general questions about how redemption provisions affect the classification of preferred stock and NCI as a liability, permanent equity or temporary equity. Additionally, the SEC staff has asked registrants how they applied specific elements of the guidance, or how a specific redemption provision was analyzed under the relevant guidance. For example, the SEC staff has asked about a registrant’s accounting policy for subsequent measurement of a redeemable noncontrolling interest, and how it complies with the measurement guidance in ASC 480-10-S99-3A.

### **Example SEC staff comment: Redeemable noncontrolling interests**

We note you classify non-redeemable noncontrolling interest in permanent equity and redeemable noncontrolling interest in temporary equity on the consolidated balance sheets. Tell us in detail and disclose your accounting policy regarding the initial recognition and measurement, subsequent measurement and classification of your redeemable and non-redeemable noncontrolling interests.

### **EY resources**

[Financial reporting developments, Derivatives and hedging](#)

[Financial reporting developments, Issuer’s accounting for debt and equity financings](#)

[Financial reporting developments, Consolidation: Determination of a controlling financial interest and accounting for changes in ownership interests](#)

# Foreign currency matters

## Disclosure of the effects of foreign currency adjustments

### *Summary of issues noted*

The SEC staff asks registrants to expand their disclosures to more comprehensively discuss and analyze the effects that foreign currency translation and remeasurement adjustments have on their financial statements. The SEC staff frequently requests registrants to quantify and describe how changes in foreign currency rates and transactions, including those with offsetting effects, affected their results of operations.

### *Analysis of current issues*

The recent comments state that registrants with material foreign operations and transactions should consider:

- ▶ Disclosing the nature and extent of the currency risks to which the company is exposed and the effects of exchange rate changes on its financial statements
- ▶ Describing in MD&A any material effects of exchange rate changes on reported revenues, costs and business practices and plans
- ▶ Quantifying the extent to which material trends in amounts are attributable to changes in the value of the reporting currency relative to the functional currency of the underlying operations and analyzing any materially different trends in operations or liquidity that would be apparent if reported in the functional currency
- ▶ Identifying the currencies of the environments in which material business operations are conducted where exposures are material
- ▶ Identifying material unhedged monetary assets, liabilities or commitments denominated in currencies other than the operation's functional currency, and describing strategies for managing currency risk

The staff continues to ask registrants to revise how they format their disclosures on foreign currency and other market risks to comply with one of the three acceptable disclosure approaches described in Item 305(a) of Regulation S-K (i.e., tabular presentation, value at risk and sensitivity analysis to hypothetical changes in market rates).

### **Example SEC staff comment: Quantitative disclosure about foreign currency exchange rate risk**

In future periodic filings, please revise your foreign currency exchange rate risk disclosures to include quantitative information in one of the formats outlined in Item 305(a)(i) through (iii) of Regulation S-K.

# Goodwill

## Impairment analysis and disclosures

The SEC staff has requested additional disclosures on reporting units at risk of impairment.

### *Summary of issues noted*

The SEC staff has requested additional information about goodwill, including:

- ▶ Disclosures about reporting units that may be at risk of goodwill impairment and the timing of impairment losses
- ▶ Information about the registrant's impairment testing policies
- ▶ Disclosure of goodwill impairment testing policies
- ▶ Information on how reporting units were identified and components were aggregated, particularly when only a single reporting unit is identified

### *Analysis of current issues*

#### *Reporting units at risk of impairment*

The SEC staff has frequently asked registrants to provide additional disclosure when the future impairment of goodwill represents a known uncertainty required to be disclosed in MD&A. In order to assist registrants in meeting this disclosure obligation, the SEC staff provides disclosures in Financial Reporting Manual (FRM) Section 9510.3 that registrants should consider when any reporting unit's estimated fair value does not substantially exceed its carrying value (i.e., the reporting unit is at risk of failing a future impairment test under ASC 350). This request is particularly common when the registrant's operating results (or that of the relevant segment) have declined significantly.

#### **Example SEC staff comment: Reporting units at risk of impairment**

To the extent that any of your reporting units have estimated fair values that are not substantially in excess of the carrying value and to the extent that goodwill for these reporting units, in the aggregate or individually, if impaired, could materially impact your operating results, please provide the following disclosures for each of these reporting units:

- ▶ Identity of the reporting unit
- ▶ The percentage by which fair value exceeds the carrying value as of the most recent impairment test
- ▶ The amount of goodwill
- ▶ A description of the methods and key assumptions used and how the key assumptions were determined
- ▶ A discussion of the degree of uncertainty associated with the key assumptions
- ▶ A discussion of any potential events and/or circumstances that could have a negative effect on the estimated fair value

The SEC staff has stated that it expects a registrant to apply judgment when determining whether the fair value is not substantially in excess of the carrying amount, and thus a reporting unit's goodwill is considered at risk. If goodwill impairment is identified as a critical accounting estimate, but the registrant does not have any reporting units that are at risk of failing the goodwill impairment test, the SEC staff expects the registrant to disclose that fact in MD&A.

The SEC staff has highlighted the importance of disclosing the percentage by which the fair value exceeded the carrying value of reporting units that are at risk of impairment as of the most recent goodwill impairment test.

The SEC staff also has challenged the timing of a goodwill impairment charge, particularly when the conditions that resulted in the charge also existed in prior periods. The SEC staff has questioned whether adequate disclosure was made in previous filings when a goodwill impairment charge was recorded for a reporting unit that was not previously disclosed as being at risk.

#### *Information on impairment analysis*

The SEC staff has asked for information about a registrant's impairment analysis, including:

- ▶ Details of the goodwill impairment analysis for each reporting unit, including how reporting units are identified and how assets, liabilities and goodwill are assigned to reporting units
- ▶ Sensitivity analyses regarding material assumptions used in testing goodwill for impairment, including qualitative and quantitative factors, and how changes in those assumptions might affect the outcome of the goodwill impairment test
- ▶ The reconciliation of the aggregate fair values of the reporting units to the registrant's market capitalization and justification of the implied control premium, including relevant transactions reviewed to support the control premium
- ▶ Details of the registrant's analysis of events that have occurred since the latest annual goodwill impairment assessment and whether those events are indicators of impairment that require an interim goodwill impairment assessment
- ▶ The reasons for and the result of any goodwill impairment test, even if no impairment was recognized
- ▶ The type of events that could lead to a future goodwill impairment

The SEC staff also has asked registrants whether they performed interim impairment tests when publicly available information indicated that such a test may have been necessary (e.g., the company's market capitalization declined, the company reduced prices, the company faced more competition). If the registrant didn't perform a test, the SEC staff has requested an explanation. The staff has also challenged the results of interim impairment testing.

The SEC staff has asked registrants to disclose additional information about their impairment analyses in critical accounting estimates in MD&A after reviewing the information provided.

### *Disclosure of accounting estimates*

The SEC staff has asked registrants to provide robust disclosures in their critical accounting estimates section in MD&A about assessing goodwill for impairment and frequently requested additional information about the facts and circumstances leading to any recognized goodwill impairment. These requests often focus on:

- ▶ The accounting policies related to the goodwill impairment tests, including when the impairment test is performed, whether the optional qualitative assessment was performed for any reporting units, how reporting units are identified and aggregated, and how goodwill is assigned to reporting units
- ▶ The facts and circumstances leading to an impairment or that could lead to a future impairment
- ▶ How the fair value of each reporting unit was estimated, including the significant assumptions and estimates used
- ▶ Reporting units with material amounts of goodwill that are at risk of future impairment

#### **Example SEC staff comment: Factors that could lead to a future impairment**

Please expand your disclosures to discuss any material uncertainties, such as operational, economic and competitive factors specific to the key assumptions underlying the fair value estimate used in your impairment testing that have a reasonable possibility of changing and could lead to additional material goodwill impairment charges in the future.

### *Identification of reporting units and aggregation of components*

A reporting unit is either an operating segment, as defined in ASC 280, or a component, which is one level below an operating segment, depending on whether certain criteria are met.

An operating segment is the highest level within a company that can be a reporting unit (i.e., the operating segment level is the ceiling), and a component is the lowest level within the company that can be a reporting unit (i.e., the component level is the floor). For further discussion on segment reporting, please refer to the *Segment reporting* section of this publication.

The SEC staff has asked registrants to clarify the number and type of reporting units (i.e., operating segments or components) identified for impairment testing and include the reasons for any changes in the number of reporting units. In particular, if a registrant has completed an acquisition or reorganization, the SEC staff has requested information on the reason for a change (or lack of change) in the number of reporting units and the effect on goodwill impairment testing.

#### **Example SEC staff comment: Identification of reporting units**

Please tell us the level at which you evaluate goodwill for impairment. We interpret your disclosures to indicate that you have only one operating segment. If our interpretation is incorrect, please clarify. If you evaluated goodwill at a component level, please explain how you determined each reporting unit and provide us a summary of the reporting units evaluated along with the related goodwill associated with each unit. If you evaluated goodwill on a single operating segment basis, please explain in detail your basis for this designation given your history of discrete business acquisitions.

#### **Example SEC staff comment: Change in reporting units**

Based on disclosures in your current- and prior-year Forms 10-K, it appears to us that there was a reduction in your reporting units from three to two. Please explain to us the reason for this change and address the effect, if any, it had on your annual goodwill impairment testing. Also, please ensure future filings adequately address any changes in reporting units.

A component of an operating segment is a reporting unit if it constitutes a business for which discrete financial information is available, and segment management regularly reviews its operating results. Segment management consists of one or more segment managers.<sup>2</sup> Two or more components in the same operating segment should be aggregated and deemed a single reporting unit if the components have similar economic characteristics.<sup>3</sup>

The SEC staff has asked registrants to clarify whether a single reporting unit exists or whether multiple components were aggregated into a single reporting unit. In the latter case, the SEC staff has asked registrants to explain the specific facts and circumstances (e.g., analysis of similar economic characteristics) that support this conclusion.

When reviewing the aggregation of components into a single reporting unit, the SEC staff considers public information available from a registrant's earnings calls and website, as well as industry and analyst presentations. The SEC staff has asked registrants to explain any perceived inconsistencies in how the businesses (i.e., components) are described in public information and how components are evaluated for aggregation into a single reporting unit.

#### **EY resources**

[Financial reporting developments, Intangibles – goodwill and other](#)

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<sup>2</sup> For purposes of ASC 350, the term "segment manager" has the same meaning as in ASC 280.

<sup>3</sup> ASC 350-20 states that ASC 280-10-50-11 must be considered when determining whether the components of an operating segment have similar economic characteristics.

# Income taxes

## Disclosures related to deferred tax assets and their realizability

### *Summary of issues noted*

The SEC staff continues to focus on valuation allowances and registrants' disclosures about their assessment of the realizability of deferred tax assets in both the financial statements and in MD&A.

In particular, the SEC staff may question the realizability of deferred tax assets recorded by registrants that have recognized consecutive annual losses or a significant loss in the current year. The SEC staff also may ask registrants to explain their reasons for reversing or significantly changing a valuation allowance if the reason is not readily apparent. Also, the SEC staff often comments if a registrant's disclosures related to its assessment of the realizability of deferred tax assets are not sufficient.

### *Analysis of current issues*

A valuation allowance is required if, based on the weight of available evidence (both positive and negative), it is more likely than not (i.e., a likelihood of more than 50%) that some portion or all of a deferred tax asset will not be realized.

There are four sources of taxable income to be considered when determining whether a valuation allowance is required (ASC 740-10-30-18). Ultimately, the realizability of deferred tax assets depends on the existence of sufficient taxable income of the appropriate character in either the carryback or carryforward period available under the tax law.

The SEC staff frequently asks registrants to provide more information about their:

- ▶ Assessment of all available positive and negative evidence used to determine the realizability of deferred tax assets, how the evidence was weighted and the extent to which the evidence was objectively verifiable
- ▶ Consideration of the four sources of taxable income, including how deferred tax liabilities are factored into the assessment, how much future taxable income the registrant would need to fully realize the deferred tax assets and the nature of any tax planning strategy that is factored into the analysis
- ▶ Deferred tax asset valuation allowance, particularly when negative evidence suggests it might be necessary or positive evidence suggests it is unnecessary
- ▶ Change in a previously recorded valuation allowance when the evidence that led to this decision is not readily apparent

Overall, the questions that the SEC staff typically raises stem from what it perceives to be inadequate or overly general (i.e., boilerplate) disclosures in the financial statements and MD&A regarding how a registrant evaluated the realizability of deferred tax assets.

As noted above, the SEC staff has asked registrants about the positive and negative evidence they considered when a valuation allowance was reversed or significantly changed if the reason for that change is not readily apparent. When determining the weight to place on each piece of evidence, registrants should consider how objectively verifiable the evidence is. By its very nature, future taxable income (exclusive of the reversal of existing temporary differences and carryforwards) requires estimates and judgments about future events.

Registrants should carefully assess the realizability of their deferred tax assets and make transparent and complete disclosures in their financial statements and MD&A about their assessment.

**Example SEC staff comment: Realizability of deferred tax assets**

We have read your disclosures which indicate that you had loss carryforwards for federal income tax purposes and that you have not provided a valuation allowance related to these carryforwards. Please provide us with a comprehensive analysis of the positive and negative evidence that you considered to determine that no valuation allowance for the federal loss carryforwards was appropriate. We note you are currently in a cumulative three-year net loss position at the end of fiscal 2016. Further, in future periodic filings, please provide a more robust description of the positive and negative evidence you consider when determining whether your deferred tax asset valuation allowance is appropriate.

**EY resources**

[Financial reporting developments, \*Income taxes\*](#)

## Income tax rate reconciliations and foreign earnings

### *Summary of issues noted*

The SEC staff continues to express concern about the clarity of registrants' income tax rate reconciliations and the transparency of their disclosures about the effect of foreign earnings on their effective tax rates. More specifically, for material rate reconciliation items associated with foreign jurisdictions, the SEC staff asks registrants to disclose which jurisdictions materially affect their effective tax rates, the tax rates in those jurisdictions and information about how the tax rates in those jurisdictions (e.g., magnitude, mix) affect the effective tax rate.

Further, the SEC staff has expressed concerns about the quality of registrants' MD&A disclosures related to income taxes. The SEC staff has indicated that the income tax disclosures in MD&A often aren't cohesive and don't tell a complete story about the company's tax positions and related trends and uncertainties. The SEC staff often asks registrants for the following information:

- ▶ Reasons for historical changes in the effective tax rate
- ▶ Discussion about changes in reconciling items between the effective and statutory tax rates
- ▶ Whether and why past income tax rates are indicative of future tax rates
- ▶ Trends and uncertainties related to changes in unrecognized tax benefits
- ▶ Reasons why certain items affect or do not affect the effective tax rate

### *Analysis of current issues*

The SEC staff reminds registrants to clearly label items in the income tax rate reconciliation. Registrants are required to provide a reconciliation between the amount of reported total income tax expense (benefit) and the amount computed by multiplying the income (loss) before tax by the applicable statutory federal income tax rate and showing the estimated dollar value of each of the underlying causes for the difference (ASC 740-10-50-12). Reconciling items that are individually less than 5% of the computed amount may be combined in the reconciliation (Article 4-08(h) of Regulation S-X).

#### **Example SEC staff comment: Income tax rate reconciliation**

We note your discussion and analysis of the changes in your effective income tax rate. Please expand your disclosures to provide a more robust analysis around the material items impacting your effective tax rate including the underlying facts and circumstances that drove those changes and whether you expect such changes to continue in the future. With reference to your tabular reconciliation, please explain the material factors impacting the Other line item that positively impacted your effective tax rate by 4% in 2017 and only 1% in 2016.

The SEC staff also questions whether large "provision to return" or "true-up" adjustments included in the income tax rate reconciliation reflect the correction of prior-year errors rather than changes in estimates.

### *Foreign earnings*

A registrant may report a relatively low effective tax rate if it derives substantial income from low-tax-rate jurisdictions. In these circumstances, the registrant's income tax reconciliation may include a large reconciling item related to these low-tax-rate jurisdictions.

The SEC staff often asks registrants to quantify and describe the nature of the significant components of the international items that affect their tax rates, including the primary international taxing jurisdictions where foreign earnings are derived, the location of tax credits and the relevant statutory rates in those jurisdictions that may affect registrants' current or future tax expense.

#### **Example SEC staff comment: Foreign earnings**

You have disclosed that the effective tax rate for 2016 was lower than the US statutory rate due to the benefit of overall lower tax rates in certain international jurisdictions as well as the benefit of certain discrete items. Please tell us and expand your disclosure to specifically identify the international jurisdictions that have impacted your rate, their respective statutory tax rates and any expectations about trends in these jurisdictions that may impact your current or future tax expense. Please also quantify any significant items that have impacted your income tax expense and expand your disclosure in management's discussion and analysis to describe any expectations about trends that may impact your current or future tax expense. Please refer to Item 303(a)(3) of Regulation S-K and SEC Release No. 33-8350.

#### ***EY resources***

[Financial reporting developments, \*Income taxes\*](#)

## Accounting for US tax reform

### *Summary of issues noted*

SEC staff members have said they are monitoring disclosures companies make under SAB 118, especially as the deadline for companies to complete their accounting for the enactment-date income tax effects of the Tax Cuts and Jobs Act (Act) approaches.

The SEC staff issued the SAB to provide guidance for registrants that could not complete their accounting for the income tax effects of the Act under ASC 740 in the period of enactment (i.e., the period including 22 December 2017). The SAB gave registrants a measurement period of up to one year to obtain, prepare and analyze the information needed and required detailed disclosures of their progress.

In a recent speech, Sagar Teotia, the SEC's Deputy Chief Accountant, noted that the SAB does not provide a deferral and said the staff expects companies to "keep moving in good faith" to complete their accounting as soon as they can. "This should not be interpreted as a window to put pencils down until we are close to one year from the enactment date to get started on the accounting," he said.

These comments suggest that the SEC staff could raise questions if a registrant records significant changes to its provisional amounts toward the end of the measurement period or has not updated provisional amounts recorded in the period of enactment. That is, the SEC staff could ask such a registrant to provide supplemental information about whether it has appropriately disclosed the material financial reporting effects of the Act for which the accounting was incomplete or request additional information supporting the timing of when the company recorded an adjustment to provisional amounts. The SEC staff has issued these types of comments in the past when registrants have made significant changes to provisional amounts recorded during the measurement period allowed in accounting for business combinations.

### *Analysis of current issues*

*SAB 118 requires companies to disclose information about the material financial reporting effects of the Act for which the accounting under ASC 740 is incomplete, including:*

- ▶ Qualitative information about the income tax effects of the Act for which the accounting is incomplete
- ▶ The items reported as provisional amounts
- ▶ Existing current or deferred tax amounts for which the income tax effects of the Act have not been completed
- ▶ The reason the initial accounting is incomplete
- ▶ The additional information that needs to be obtained, prepared or analyzed to complete the accounting requirements under ASC 740
- ▶ The nature and amount of any measurement period adjustments recognized during the reporting period

Further, we understand that the SEC staff expects a company that has elected to account for global intangible low-taxed income (GILTI) as part of deferred taxes, but is still evaluating its accounting method for measuring those deferred tax amounts, to disclose that its method for measuring GILTI is provisional and may be changed during the measurement period. Similarly, when a company has not yet elected an accounting policy for GILTI during the SAB 118 measurement period, it should disclose that it is still evaluating the Act's GILTI provisions and has not yet elected an accounting policy.

In light of the US tax reform, registrants must also consider MD&A disclosure for any material short- and long-term liquidity implications of paying the required one-time transition tax on their accumulated foreign earnings on which they have previously deferred the US income taxes.

Mr. Teotia said in his speech that a company's disclosures during the measurement period provide important information to users of the financial statements and are a meaningful component of SAB 118.

#### ***EY resources***

[\*Technical Line, A closer look at accounting for the effects of the Tax Cuts and Jobs Act\*](#)

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# Intangible assets

## Recognition, measurement, amortization and impairment

### *Summary of issues noted*

The SEC staff has requested that registrants provide the following details about their intangible asset disclosures:

- ▶ Information about intangible assets recognized as part of a business combination
- ▶ An explanation of how the useful lives were determined, and for finite-lived intangible assets (e.g., customer relationships) the factors leading to the amortization method selected
- ▶ Supplemental information on how intangible assets were assessed for impairment

After reviewing this information, the SEC staff has asked registrants to enhance or revise their intangible asset disclosures.

### *Analysis of current issues*

#### *Intangible assets recognized in a business combination*

ASC 805 requires a registrant to determine the fair value of identifiable assets acquired (with certain limited exceptions), including intangible assets that (1) arise from contractual or other legal rights or (2) are separable.

The SEC staff's comments have focused on the values assigned to specific identifiable intangible assets, as well as the significant estimates and assumptions used in calculating fair value measurements and the subsequent accounting for such recognized intangibles. Specifically, the SEC staff has requested that registrants discuss in MD&A the valuation method and principal assumptions they used to determine the fair value of each major class of intangible assets acquired.

#### *Useful life determination – indefinite-lived intangible assets*

When determining the useful life of an intangible asset, a registrant should consider the period over which the asset is expected to contribute directly or indirectly to its future cash flows. Registrants should consider all of the factors listed in ASC 350 and all other relevant information when determining the useful lives of intangible assets.

The SEC staff has asked how a registrant has considered its own historical experience in renewing or extending similar arrangements (consistent with the intended use of the asset by the registrant). A registrant should consider its own historical experience even if similar arrangements did not have explicit renewal or extension provisions.

A registrant should consider the useful life of an intangible asset to be indefinite only after considering all relevant facts and determining that there are no legal, regulatory, contractual, competitive, economic or other factors that limit the useful life of the intangible asset. The SEC staff also has challenged a registrant's assertions that intangible assets have an indefinite life and has asked registrants to explain the factors they considered when making this determination.

**Example SEC staff comment: Useful life determination – indefinite-lived intangible assets**

Tell us how you determined that the acquired intangible assets from your acquisition of ABC Company were deemed to have an indefinite useful life. In your response, please tell us why you believe that no legal, regulatory, contractual, competitive, economic, expected use or other factors could limit the useful life of these intangible assets. We refer you to ASC 350-30-35-1 through 4.

*Useful life determination and amortization method – finite-lived intangible assets*

The SEC staff focuses on the useful life and amortization method of acquired finite-lived intangible assets (e.g., trade names, customer lists, customer contracts, customer relationships). The SEC staff has asked registrants to disclose how they determined the useful life of these assets and challenged such useful lives when the underlying assumptions do not appear consistent with information disclosed in other areas of the filing. The SEC staff also has inquired about the amortization method chosen for these assets (e.g., straight-line versus accelerated) and requested that registrants explain their key assumptions about the expected future cash flows from an acquired intangible asset to support their chosen amortization method.

**Example SEC staff comment: Useful life determination – finite-lived intangible assets**

Please help us better understand how you determined the 36-year period over which the acquired customer relationships are expected to contribute directly or indirectly to your future cash flows. Tell us in more detail about the attrition analysis of the customer relationships acquired, including, but not limited to, the historical length of those relationships and rates of attrition. Also tell us how contractual renewals and other extensions were considered in your analysis. Describe your own historical experience renewing or extending similar arrangements and how it affected your analysis and what, if any, market participant assumptions were considered and incorporated into your conclusion. In this regard, we note from your disclosures that the useful lives of customer relationships acquired in prior periods range from five to ten years for the fiscal year ended December 31 and that most of your contracts have terms ranging from three to five years, including renewal terms at the option of the customer.

The SEC staff has challenged whether impairments of indefinite-lived intangibles should be recognized if a registrant's market capitalization or operating results (or the operating results of the relevant segment) have declined significantly.

#### **Example SEC staff comment: Amortization method – finite-lived intangible assets**

We note that you amortize other intangible assets, including customer relationships, on a straight-line basis over their estimated useful lives of 20 years. Customer relationships generally dissipate at a more rapid rate in the earlier periods following a company's succession to these relationships, with the rate of attrition declining over time. Under this pattern, a significant amount of cash flows derived from the acquired customer base may be recognized in earlier periods and then fall to a materially reduced level in later years. Please tell us why you believe that the straight-line method of amortization rather than an accelerated method reflects the pattern in which the economic benefits are consumed or explain why you cannot reliably determine the pattern in accordance with ASC 350-30-35-6.

#### *Supplemental information on impairment analysis*

An indefinite-lived intangible asset should be tested for impairment annually or more frequently (in accordance with ASC 350) if events or changes in circumstances indicate that the asset might be impaired. The SEC staff has requested that registrants explain how indefinite-lived intangible assets are tested for impairment, including the valuation method and significant assumptions used to determine the estimated fair values of the assets. As it has done with goodwill impairment, the SEC staff has challenged whether impairments of indefinite-lived intangibles should be recognized when the market capitalization or operating results of the registrant (or of the relevant segment) have declined significantly.

When a goodwill or long-lived asset impairment charge has been incurred, the SEC staff has requested an explanation of how the registrant considered the factors that led to impairment in evaluating the need for an impairment test of other finite-lived intangible assets in the period. Additionally, if a registrant doesn't record an impairment charge when other companies in the same industry or market are experiencing an economic downturn and recognizing impairment charges, the SEC staff is more likely to request an explanation.

#### **EY resources**

[Financial reporting developments, \*Intangibles – goodwill and other\*](#)

[Financial reporting developments, \*Business combinations\*](#)

# Revenue recognition

## ***ASC 606, Revenue from Contracts with Customers, and ASC 340-40, Other Assets and Deferred Costs – Contracts with Customers***

### ***Overview***

Comment letters that were issued to certain early adopters of ASC 606 and ASC 340-40 are now public and may provide an indication of the types of comments the SEC staff is issuing to registrants that adopted the new standard this year. This section will focus on those comments and highlight emerging topics.

As expected, the SEC staff's comments on the application of ASC 606 and ASC 340-40 have focused on areas of judgment (e.g., identifying performance obligations, determining timing of satisfaction of performance obligations, determining the amortization period of capitalized contract costs). Based on what we have seen, registrants appear to have been able to resolve these comments in the same manner as comments on other topics. That is, the registrants have helped the staff gain a better understanding of the judgments made by management or provided additional disclosures in future filings. Contemporaneous documentation of the judgments made in applying ASC 606 and ASC 340-40 will help facilitate the dialogue with the SEC staff during the comment process.

For trends regarding ASC 605, please refer to the 2017 SEC Comments and Trends publication since current-year trends are generally consistent with last year's trends.

### ***EY resources***

[Financial reporting developments, \*Revenue from contracts with customers\* \(ASC 606\)](#)

## Identifying performance obligations

The SEC staff has asked registrants how they determined their performance obligations in contracts with customers.

### *Summary of issues noted*

The SEC staff has asked registrants how they determine their performance obligations in contracts with customers. In particular, the SEC staff is interested in how registrants support their conclusions that certain promised goods and services are not separately identifiable.

### *Analysis of current issues*

To apply ASC 606, an entity must first identify the promised goods and services within a contract with a customer and then determine which of those goods and services are separate performance obligations. Promised goods and services represent separate performance obligations if the goods or services are distinct (by themselves or as part of a bundle of goods and services) or if the goods and services are part of a series of distinct goods and services that are substantially the same and have the same pattern of transfer to the customer.

A promised good or service is distinct if both of the following criteria are met: (1) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e., the good or service is capable of being distinct), and (2) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (i.e., the promise to transfer the good or service is distinct within the context of the contract). If a promised good or service does not meet the criteria to be considered distinct, it is required to be combined with other promised goods or services until a distinct bundle of goods or services exists.

The SEC staff has requested that registrants provide an analysis supporting their determination that certain promised goods or services in a contract were not separately identifiable from other promises in the contract and, therefore, were not distinct performance obligations.

### **Example SEC staff comment: Identifying performance obligations**

We note some of your contracts have multiple performance obligations. Please tell us and revise to disclose the nature of these performance obligations pursuant to ASC 606-10-50-12(c). For maintenance, support and warranty services, please provide us with your analysis as to why these services were not separately identifiable in accordance with the guidance of ASC 606-10-25-21, as applicable.

Registrants should carefully identify the promises in a contract and evaluate the criteria for determining whether the promised goods and services are separately identifiable from other promises in the contract (i.e., whether the promise to transfer the good or service is distinct in the context of the contract), which may require significant judgment. ASC 606-10-25-21 includes three factors that are intended to help entities determine when the promises in a bundle of promised goods or services are not separately identifiable and, therefore, should be combined into a single performance obligation: (1) the presence of a significant integration service, (2) the presence of significant modification or customization or (3) the promised goods or services are highly interdependent or highly interrelated.

Thorough and contemporaneous documentation of this analysis is critical to determine the performance obligations (i.e., the unit of account for revenue recognition) in a contract with a customer.

Registrants should review their disclosures to verify that they meet the requirement of ASC 606-10-50-12(c) which states that an entity shall disclose information about its performance obligations in contracts with customers, including a description of the nature of the goods or services that the entity has promised to transfer.

***EY resources***

[Financial reporting developments, \*Revenue from contracts with customers\* \(ASC 606\)](#)

## Satisfaction of performance obligations

### *Summary of issues noted*

The SEC staff has asked registrants why the method they used to measure progress toward satisfaction of an over time performance obligation provides a faithful depiction of the transfer of goods or services in a contract with a customer.

### *Analysis of current issues*

When an entity has determined that a performance obligation is satisfied over time, ASC 606 requires the entity to select a single revenue recognition method (i.e., measure of progress) that depicts the entity's performance in transferring control of the goods or services. The standard provides two methods for measuring progress: (1) input methods (e.g., resources consumed, labor hours expended, costs incurred, time elapsed, machine hours used) and (2) output methods (e.g., surveys of performance completed to date, appraisals of results achieved, milestones reached, time elapsed, units produced or units delivered).

ASC 606-10-50-18(b) requires entities to disclose the method used to recognize revenue (e.g., a description of the input or output methods used and how those methods are applied) and why the method selected provides a faithful depiction of the transfer of goods or services. The SEC staff has commented when registrants have not included the latter disclosure.

### **Example SEC staff comment: Satisfaction of performance obligations**

You disclose you recognize revenue over time using an input measure (e.g., costs incurred to date relative to total estimated costs at completion). Revise to disclose why this method is a faithful depiction of the transfer of goods or services pursuant to ASC 606-10-50-18(b).

In determining the method of measuring progress that faithfully depicts an entity's performance, the entity should consider both the nature of the promised goods or services and the nature of the entity's performance. In other words, an entity's selection of the method used to measure its performance should be consistent with the nature of its promise to the customer and what the entity has agreed to transfer to the customer.

Registrants should review their disclosures to verify that they not only meet the specific requirements of ASC 606-10-50-18(b) but also meet the overall objective discussed above.

### **EY resources**

[Financial reporting developments, Revenue from contracts with customers \(ASC 606\)](#)

## Disaggregated revenue disclosures

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The SEC staff has asked about registrants' disaggregated revenue disclosures and how categories for disaggregation were determined.

### *Summary of issues noted*

The SEC staff has asked about registrants' disaggregated revenue disclosures and how the categories for disaggregation were determined in accordance with the disclosure requirements in ASC 606.

### *Analysis of current issues*

In accordance with the disclosure requirements in ASC 606-10-50-5, registrants are required to disclose disaggregated revenue information to illustrate how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

The implementation guidance in ASC 606 (i.e., ASC 606-10-55-89 through 55-91) indicates that the most appropriate categories for a particular entity will depend on its facts and circumstances, but an entity should consider how it disaggregates revenue in other communications (e.g., press releases, information regularly reviewed by the chief operating decision maker for evaluating the financial performance of operating segments) when determining which categories are most relevant and useful.

While ASC 606 does not specify how revenue should be disaggregated, the implementation guidance suggests categories for entities to consider. Example categories include, but are not limited to, all of the following:

- ▶ Type of good or service (e.g., major product lines)
- ▶ Geographical region (e.g., country or region)
- ▶ Market or type of customer (e.g., government and nongovernment customers)
- ▶ Type of contract (e.g., fixed-price and time-and-materials contracts)
- ▶ Contract duration (e.g., short-term and long-term contracts)
- ▶ Timing of transfer of goods or services (e.g., revenue from goods or services transferred to customers at a point in time versus over time)
- ▶ Sales channels (e.g., goods sold directly to consumers and goods sold through intermediaries)

The SEC staff has requested that registrants explain how they considered the implementation guidance in ASC 606-10-55-89 through 55-91 when selecting the appropriate categories to disaggregate revenue. Specifically, the SEC staff would like to understand how the registrant's disclosures meet the objective of depicting how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors. Similar to how it reviews segment disclosures, the SEC staff may review all publicly available information to evaluate whether the objectives of this disclosure requirement have been met.

**Example SEC staff comment: Disaggregated revenue disclosures**

We note your presentation of disaggregated revenue by major source on page XX. With respect to the disclosure requirements of ASC 606-10-50-5, please tell us how you considered the guidance in paragraphs ASC 606-10-55-89 through 55-91 in selecting the appropriate categories to use to disaggregate revenue. Please tell us why you believe your current disclosures meet the objective of depicting how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

We believe that when determining categories for disaggregation of revenue, registrants should analyze specific risk factors for each of their revenue streams to determine the proper level of revenue disaggregation that will be beneficial to users of the financial statements. If certain risk factors could lead to changes in the timing of revenue recognition, those factors should be evaluated as potential categories for this disclosure.

In addition, an entity is required by ASC 606-10-50-6 to explain the relationship between the disclosure of disaggregated revenue and revenue information that is disclosed for each reportable segment. Registrants should review their disclosures to verify that they meet this disclosure requirement.

***EY resources***

[Financial reporting developments, Revenue from contracts with customers \(ASC 606\)](#)

## Significant payment terms

### *Summary of issues noted*

The SEC staff has asked registrants to disclose significant payment terms in contracts with customers, as well as how the timing of satisfaction of registrants' performance obligations relates to the typical timing of payment.

### *Analysis of current issues*

ASC 606-10-50-12(b) states that an entity has to disclose information about its performance obligations in contracts with customers, including a description of significant payment terms. This could include when payment typically is due, whether the contract has a significant financing component, whether the consideration amount is variable and whether the estimate of variable consideration is typically constrained.

Further, ASC 606-10-50-9 requires that an entity explain how the timing of satisfaction of performance obligations relates to the typical timing of payment, as well as the effect those factors have on the contract asset and liability balances. Under ASC 606, a contract asset or contract liability is generated when either party to a contract performs, depending on the relationship between the entity's performance and the customer's payment. When an entity satisfies a performance obligation by transferring a promised good or service, the entity has earned a right to consideration from the customer and, therefore, has a contract asset. When the customer performs first (e.g., by prepaying its promised consideration), the entity has a contract liability.

The SEC staff has commented when registrants have not included a robust disclosure of their significant payment terms.

### **Example SEC staff comment: Significant payment terms**

Tell us your significant payment terms and how the timing of satisfaction of performance obligations relates to the timing of payment and the effect on the contract asset and liability balances. Disclose the information required by ASC 606-10-50-9 and 50-12(b) in future filings.

Registrants should review their disclosures to verify that they meet the disclosure requirements in ASC 606-10-50-12(b) and ASC 606-10-50-9.

### ***EY resources***

[Financial reporting developments, Revenue from contracts with customers \(ASC 606\)](#)

## Amortization of capitalized contract costs

The SEC staff has asked registrants to explain how they determined the amortization period for contract costs capitalized under ASC 340-40.

### *Summary of issues noted*

The SEC staff has asked registrants to explain how they determined the amortization period for contract costs capitalized under ASC 340-40. In particular, the SEC staff asks for more information about costs to obtain a contract with a customer, including how renewal sales commissions (if any) are considered in the amortization period determination.

### *Analysis of current issues*

Under ASC 340-40, the incremental costs of obtaining a contract with a customer (e.g., sales commissions) are recognized as an asset if the entity expects to recover those costs. Any capitalized contract costs are amortized over a period that is consistent with the transfer to the customer of the related goods or services. This can also be thought of as the expected period of benefit of the asset capitalized that likely would extend beyond the contract term if the capitalized contract costs relate to goods or services being transferred under multiple contracts or to a specific anticipated contract (e.g., certain contract renewals).

When evaluating whether the amortization period for an initial sales commission extends beyond the original contract period, an entity should evaluate whether an additional commission is paid for any expected renewals and, if so, whether the renewal commission is “commensurate” with the original commission (i.e., reasonably proportional to the contract values). For example, a 6% commission on an initial contract and a 2% commission on a renewal would not be commensurate. If the entity’s past experience indicates that a renewal is likely, the amortization period would be longer than the initial term if the renewal commission is not commensurate with the initial commission.

When the expected period of benefit extends beyond the initial contract term, it may be the expected customer relationship period, but that is not always the case. To determine the appropriate amortization period, an entity will need to evaluate the type of capitalized costs, what the costs relate to and the specific facts and circumstances of the arrangement.

When evaluating the appropriate amortization period for renewal commissions, an entity would also consider whether additional commissions are expected for further renewals and whether those commissions would be commensurate. For example, if an entity expects to renew an annual contract in years two through four and pay a 2% commission upon each renewal, each renewal commission would be considered commensurate, and the appropriate amortization period for each renewal commission would likely be one year.

The SEC staff has requested that registrants provide more information about capitalized costs to obtain a contract with a customer. Specifically, the SEC staff has asked whether additional sales commissions are paid for contract renewals, if those renewal commissions are commensurate with the initial commissions and how expected renewals are considered when determining the amortization period for commissions capitalized under ASC 340-40. In addition, the staff has also asked about how renewal commissions are amortized. The SEC staff also asks registrants to include such information in their disclosures in accordance with ASC 340-40-50-2(b).

#### **Example SEC staff comment: Amortization of capitalized contract costs**

Please tell us, and revise to clarify if appropriate, whether additional sales commissions are paid upon contract renewal and, if so, whether such amounts are commensurate with the initial commissions. Please also disclose how commissions paid for renewals are considered in your five-year period of benefit for the initial commission. Finally, please disclose the period of time over which you amortize commission costs related to contract renewals. Refer to ASC 340-40-35-1 and 340-40-50-2(b).

In determining the appropriate amortization period or the period of benefit for capitalized contract costs, the entity should consider its facts and circumstances and may use similar judgment to that used when estimating the amortization period for intangible assets (e.g., a customer relationship intangible acquired in a business combination). This could include considering factors such as customer “stickiness” and how quickly the entity’s products and services change. It will be important for registrants to document the judgments made when determining the appropriate amortization period.

ASC 340-40 disclosure requirements include judgments made in determining the amounts of costs that are capitalized, the amortization method chosen and other quantitative disclosures. Registrants should review their disclosures to verify that they meet the requirements in ASC 340-40-50-2(b).

#### ***EY resources***

[Financial reporting developments, \*Revenue from contracts with customers\* \(ASC 606\)](#)

# Segment reporting

## Identification and aggregation of operating segments, disclosures and internal control over financial reporting

### *Summary of issues noted*

The SEC staff continues to focus on segment reporting and how registrants apply ASC 280. The areas the SEC staff is focusing on include:

- ▶ How registrants identify operating segments
- ▶ How registrants aggregate operating segments into reportable segments
- ▶ Whether registrants provide appropriate disclosures, including general information disclosures, reconciliations and entity-wide disclosures related to products and services, revenues attributable to individual foreign countries and revenues from major customers
- ▶ Whether registrants have inappropriately included non-GAAP measures in their segment disclosures

### *Analysis of current issues*

The SEC staff continues to focus on segment disclosures and the application of ASC 280, including the basic objectives and principles outlined in the segment reporting guidance.

The SEC staff has emphasized the importance of ICFR including whether the design and operation of internal controls over a registrant's segment reporting judgments are appropriate. The SEC staff has said that the guidance on segment reporting requires a registrant to apply reasonable judgment. Therefore, input from, and interaction with, the chief operating decision maker (CODM) may be an important element in the design of effective internal controls over financial reporting, specifically how the CODM allocates resources and assesses performance.

The SEC staff also has reminded registrants that documenting the design and effective operation of management's controls over these judgments is an integral part of management's support for the effectiveness of its ICFR and is essential to the auditor's ability to evaluate these controls.

When reviewing segment reporting, the SEC staff considers information within the registrant's public filings as well as information available from a registrant's earnings calls, website and industry or analyst presentations. The SEC staff has asked registrants to explain any inconsistencies between how the business is described in public information and how it is described in their segment footnotes. For example, the SEC staff has challenged registrants when they say the basis for identifying operating segments is something other than product or service lines (e.g., geography) but publicly disclosed information suggests that management uses financial information by product or service lines to make decisions and allocate resources.

The SEC staff expects registrants to continually monitor business developments and has inquired about changes in the business that could affect the identification or aggregation of operating segments.

The SEC staff continues to challenge assessments made under ASC 280.

While the SEC staff has historically commented on segment reporting, we continue to see a high level of focus in this area, even when the SEC staff has previously commented on a registrant's segment reporting. Questions on segment reporting have often resulted in multiple rounds of comments, particularly when the registrant's initial response was not comprehensive. The review process also has led to requests for a teleconference with the SEC staff, including representatives of the SEC's Office of the Chief Accountant.

#### *Identification of operating segments*

The segment reporting guidance is based on a "management approach" (ASC 280-10-5). That is, segment disclosures should be consistent with a registrant's internal management reporting structure to enable investors to view the registrant similarly to the way management does. Registrants should challenge any conclusions they reach on operating segments that are not consistent with the basic organizational structure of their operations. To support the management approach concept, the SEC staff has requested that registrants include a discussion of their internal structure or an organizational chart and the processes used to make operating decisions in their comment letter responses.

Identifying operating segments (ASC 280-10-50-1 through 50-9) is the first step in preparing segment disclosures. A critical element of this analysis is identifying the CODM. Under ASC 280, the CODM is a function, not necessarily a manager with a specific title. The SEC staff has said that a registrant should focus on who makes the key operating decisions in the organization and not default to who makes the strategic decisions or has the ultimate decision-making authority. That is, the registrant should not default to the chief executive officer or the chief operating officer when determining the CODM, and the registrant's ICFR should identify and assess those responsible for the key operating decisions that are necessary to run the business.

To evaluate a registrant's identification of operating segments, the SEC staff often requests a description of the registrant's organizational structure and detailed information about employees who report directly to the CODM, including their roles and responsibilities and interactions with the CODM. The SEC staff also considers the basis on which budgets and forecasts are prepared and how performance objectives are evaluated, including how executive compensation is determined (e.g., performance criteria underlying compensation plans). This information allows the SEC staff to challenge whether the identified operating segments are consistent with how the CODM assesses performance and allocates resources.

To qualify as an operating segment, a component must have discrete financial information available that the CODM uses to assess performance and make resource allocation decisions. This financial information must be sufficiently detailed to allow the CODM to make decisions. When determining whether discrete financial information is available, the SEC staff has cautioned that a registrant shouldn't conclude that discrete financial information is not available simply because certain costs are shared and not allocated specifically to each component. Gross profit information or other operating measures provided to the CODM and used to assess performance and make resource allocation decisions could be considered discrete financial information.

The SEC staff frequently has requested that registrants describe the financial information provided to the CODM so the SEC staff can understand the information used by the CODM to assess performance and allocate resources. However, the SEC staff has clarified that the fact that information is included in a reporting package is not the only factor it considers in its assessment of identified operating segments.

Further, when a registrant identifies only one operating segment, the SEC staff has challenged how decisions can be made about performance and resources for the company as a whole without evaluating discrete financial information on a more disaggregated basis. The SEC staff has said that if the application of the guidance in ASC 280 results in the identification of a single operating segment, a registrant should disclose that it allocates resources and assesses financial performance on a consolidated basis and explain the basis for that management approach.

#### **Example SEC staff comment: Identification of operating segments**

Please tell us who your CODM is and provide us with your analysis in determining the CODM. As part of your response, please provide us with an organizational chart that includes the titles and roles of the individuals who report directly to the CODM. In doing so, specifically explain to us the responsibilities of these individuals and the manner in which they typically interact with the CODM. In addition, please respond to the following:

- ▶ Tell us the nature of the resource allocation and performance assessment decisions the CODM makes, including examples to illustrate the description.
- ▶ Describe the information regularly provided to the CODM and how frequently it is prepared.
- ▶ Describe the information regularly provided to the Board of Directors and how frequently it is prepared.
- ▶ Explain how budgets are prepared, who approves the budget at each step of the process, the level of detail discussed at each step and the level at which the CODM makes changes to the budget. Also describe the level of detail communicated to the CODM when actual results differ from budgets and who is involved in the meetings with the CODM to discuss budget-to-actual variances.
- ▶ Describe the basis for determining the compensation of the individuals that report to the CODM.

Identifying operating segments also affects goodwill impairment testing. As discussed in the *Goodwill* section of this publication, the SEC staff has requested information about how a registrant identifies its reporting units. If a registrant incorrectly identifies operating segments, this could cause a registrant to incorrectly identify reporting units used in goodwill impairment testing.

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## The SEC staff considers meeting the criteria to aggregate operating segments a high hurdle.

### *Aggregation of operating segments*

ASC 280 allows, but does not require, a registrant to aggregate operating segments for reporting purposes. To aggregate operating segments, a registrant must determine that all three criteria in ASC 280-10-50-11 are met. The criteria, which all require the use of judgment, are:

- ▶ The aggregation must be consistent with the objective and basic principles of ASC 280.
- ▶ The operating segments must be economically similar.
- ▶ The following five qualitative characteristics of the operating segments must be similar: (1) the nature of the products and services, (2) the nature of the production processes, (3) the type or class of customer for their products and services, (4) the methods used to distribute their products or provide their services and (5) the nature of the regulatory environment, if applicable.

To be consistent with the objective and basic principles of ASC 280, the aggregation of operating segments should help users of the financial statements make better-informed judgments about the registrant by improving their understanding of the registrant's performance and their assessment of the prospects for future net cash flows. That is, a registrant may aggregate operating segments only if reporting them separately will not add significantly to the investor's understanding of the entity because the segments' characteristics are so similar that they can be expected to have essentially the same future prospects.

It's important to understand that while the identification of operating segments follows a management approach, the aggregation of operating segments should be viewed from the investor's perspective. The SEC staff has said that it is important for registrants to consider information such as industry reports and other analyses by users of the financial statements that may provide evidence of how a reasonable investor would analyze the company.

ASC 280 requires that aggregated operating segments have "similar economic characteristics," such that they would be expected to have similar long-term financial performance. The similarity of the economic characteristics should be evaluated based on both current performance and future projections (ASC 280-10-55-7A). However, the SEC staff has said that the expectation that operating segments will have similar economic characteristics (e.g., long-term average gross margins) in the future does not take precedence over a lack of similarity in their current and past performance.

The SEC staff often reviews the registrant's website, analyst presentations and information in public filings and raises questions if any of that information is inconsistent with the registrant's conclusion that aggregating operating segments is appropriate. For example, a discussion of diverging trends or differing results at two business lines could indicate that these two business lines, if they qualify as operating segments, may not be economically similar.

The SEC staff has requested historical and projected operating margins, gross margins, revenues and other measures of operating performance when challenging a registrant's aggregation of operating segments.

When a registrant has aggregated operating segments into a reportable segment, the SEC staff has frequently asked for an explanation of why the registrant believes the five qualitative characteristics of the operating segments are similar, as required by ASC 280.

The SEC staff also has reminded registrants that the guidance on determining whether two operating segments are similar requires a company to consider the range of its business activities and the economic environment in which it operates. For example, while a registrant with a diversified product portfolio may consider certain products similar, a registrant with a more narrow range of activities may not consider those same products similar.

In addition, the SEC staff has asked why a company's organizational structure caused it to identify separate operating segments and whether those reasons provide evidence that the operating segments are not similar.

#### **Example SEC staff comment: Aggregation of operating segments**

We note that your five operating segments are aggregated into one reportable segment. Please address the following:

- ▶ Compare and contrast your operating segments relative to the areas listed in ASC 280-10-50-11(a) through (e). With respect to any differences among your operating segments, tell us why you determined that disaggregation was not warranted.
- ▶ Provide us with each operating segment's historical and projected revenues, gross margin, operating margin and measure of segment profitability.
- ▶ Tell us the basis of organization (i.e., why the company is organized in the manner that it is).

#### *Ongoing assessment of reportable segments*

The SEC staff has challenged registrants' identification and aggregation of operating segments when there have been changes to the business. We believe this is linked to the SEC staff's emphasis on registrants having processes in place to continuously reassess their conclusions because circumstances may change over time. For example, the SEC staff has inquired about how a change in a registrant's internal reporting due to a significant acquisition, a restructuring or changes in performance among operating segments affected segment reporting conclusions.

The SEC staff may challenge whether a registrant has inappropriately included a non-GAAP measure in its segment disclosures.

**Example SEC staff comment: Identification and aggregation of operating segments including a recent acquisition**

We note your disclosure that you have determined it appropriate to aggregate your operating segments into one reportable segment. Please tell us the consideration given by management in determining your reportable segment in light of the acquisition of XYZ Company (XYZ), which operates in a different region of the country. We note from XYZ's website that it appears to continue to operate as a separate entity under the XYZ name. In this regard, please tell us how you considered these characteristics of XYZ's operations in determining that it is appropriate to present one reportable segment. Your response should address how you identified the operating segments under ASC 280-10-50-1 and 280-10-50-3 through 50 and further, how you evaluated each of the aggregation criteria in ASC 280-10-50-11.

*Disclosures*

General disclosures

ASC 280-10-50-21 requires registrants to disclose the factors they used to identify their reportable segments, including whether operating segments have been aggregated. If a registrant has not included this information in the segment footnote, the SEC staff has asked the registrant whether it has aggregated operating segments when determining reportable segments and has asked it to expand its disclosure in future filings. ASC 280-10-50-21 also requires disclosure of the types of products and services from which each reportable segment derives its revenues. The SEC staff has asked registrants to expand their disclosures when the information is not provided or does not include enough detail.

Reconciliations

ASC 280-10-50-30 requires registrants to provide reconciliations of the reportable segments' total revenues, measure of profit or loss, assets and other significant items, if disclosed, to the corresponding consolidated amounts. The SEC staff has asked registrants to revise their disclosures if they have not disclosed the reconciliations in the consolidated financial statements. The SEC staff also has asked registrants about amounts included in an "other" reconciling item, since ASC 280-10-50-31 requires significant reconciling items to be separately identified and described.

Non-GAAP measures

By definition, a segment measure of profit or loss that a company is required to disclose in accordance with ASC 280 (i.e., a measure that is reported to the CODM for purposes of making decisions about allocating resources to the segment and assessing its performance) is not a non-GAAP measure and is not subject to the rules and regulations on the use of non-GAAP financial measures.

The SEC staff's C&DIs on the use of non-GAAP financial measures address this point. The C&DIs say "because [ASC 280] requires or expressly permits the footnotes to the company's consolidated financial statements to include specific additional financial information for each segment, that information also would be excluded from the definition of non-GAAP financial measures."

However, the SEC staff may challenge whether a registrant has inappropriately included a non-GAAP measure in its segment disclosures. For example, registrants should be aware that a consolidated measure of segment profit may create a non-GAAP financial measure.

**Example SEC staff comment: Non-GAAP measures in the segment footnote**

While we note that your CODM uses segment operating income (loss) and segment operating margin percentage to evaluate segment performance, the format and labeling of your presentation include non-GAAP measures that are not measures of segment performance and you are not allowed to present them in your financial statements pursuant to Item 10(e)(1)(ii)(C) of Regulation S-K. The amounts you present in the consolidated column for operating income (loss) and operating margin percentage are not amounts presented on your statement of income or which can be directly calculated therefrom. While you may present the total of profit or loss of individual segments as part of the reconciliation required by ASC 280-10-50-30(b), such presentations must be correctly labeled and the reconciliations should be to the consolidated amounts presented in your financial statements. Please revise the format and labeling of your presentation to eliminate the non-GAAP measures consolidated operating income (loss) and consolidated operating profit margin percentage. See also Question 104.04 of the Compliance & Disclosure Interpretations for Non-GAAP Financial Measures.

The SEC staff also has said that registrants should not attempt to circumvent the non-GAAP rules by disclosing multiple measures of a segment's profit or loss in their financial statements. Similarly, the SEC staff may challenge a registrant that discloses a measure of segment profit or loss when it discloses only one reportable segment.

For further discussion, please refer to the *Non-GAAP measures* section of this publication.

*Entity-wide disclosures*

Disaggregated revenue by product and service

ASC 280 also requires a registrant to disclose the revenues it derived from transactions with external customers for each product or service or each group of similar products or services, if this information is not already provided as part of the segment information required by the standard. Entities that have only one reportable segment also are required to disclose such products and services revenues. For example, a registrant with one reportable segment that sells consumer products and provides services would be required to disclose the revenues from each significant product line or service, or groups of similar products or services, in its segment disclosure.

### **Example SEC staff comment: Disaggregated revenue by product**

Please revise to disclose revenues from external customers for each product and service or each group of similar products and services. As part of your response, please describe the similarities and differences between the products and services presented as a group. Please refer to ASC 280-10-50-40.

The SEC staff often has asked registrants that have not disclosed disaggregated revenue information to do so or explain why such disclosure was not necessary. The SEC staff has challenged the absence of such a disclosure when the registrant's publicly disclosed information indicates that its reportable segments contain a range of products or services. The SEC staff also has questioned the absence of such a disclosure when a registrant has asserted that providing the disclosure was impracticable but the information was provided elsewhere (e.g., MD&A, earnings calls).

#### Disaggregated revenue by geography

ASC 280 requires a registrant to disclose certain revenue information attributed to its country of domicile and foreign countries. A registrant also is required to disclose this revenue information for each foreign country (ASC 280-10-50-41(a)) if it is material. The SEC staff has asked registrants to disclose revenues attributed to specific countries in light of their other disclosures about foreign locations.

#### Revenue contributed by significant customers

ASC 280-10-50-42 requires registrants to disclose the total revenue from each major customer (i.e., one that contributes 10% or more of total revenues) and the segment(s) in which the revenues are reported. The SEC staff has requested that registrants disclose such information when other disclosures indicate that there may be a concentration of sales to a particular customer.

#### ***EY resources***

*Compendium of significant accounting and reporting issues, 2016 AICPA National Conference on Current SEC and PCAOB Developments*

*Financial reporting developments, Segment reporting – Accounting Standards Codification 280*

# Share-based payments

## Presentation and disclosure

### *Summary of issues noted*

The SEC staff comments when a registrant has omitted disclosures required by ASC 718 (e.g., general terms of an award, method used for measuring compensation cost from an award) and it is unclear to the staff why the disclosures were omitted.

### *Analysis of current issues*

#### *Required disclosures*

ASC 718-10-50-1 requires a registrant with one or more share-based payment arrangements to disclose information that enables users of the financial statements to understand: (1) the nature and terms of such arrangements that existed during the period and the potential effects of those arrangements on shareholders, (2) the effect of compensation cost arising from share-based payment arrangements on the income statement, (3) the method of estimating the fair value of the goods or services received, or the fair value of the equity instruments granted (or offered to grant), during the period and (4) the cash flow effects resulting from share-based payment arrangements. Although ASC 718 appears to take a principles-based approach to disclosure requirements, the guidance in ASC 718-10-50-2 includes several pages of detailed disclosure requirements described as the “minimum information” required to achieve these disclosure objectives.

The SEC staff often comments when a registrant omits a disclosure identified by ASC 718-10-50-2. If a registrant has not provided a required disclosure, the SEC staff often asks the registrant to explain and generally will not object if the omitted information is immaterial.

#### **Example SEC staff comment: Required disclosures**

Please tell us why you have not provided the disclosures required by ASC 718-10-50-2 for your stock-based compensation plans.

#### *EY resources*

[Financial reporting developments, \*Share-based payment\*](#)

# Appendix A: Industry supplements

## Insurance supplement

In this supplement, we analyze trends in SEC staff comment letters to registrants in the insurance industry. The following table summarizes the topics that the SEC staff focused on most often in comment letters sent to insurance registrants. Many of these topics are frequent areas of comment in letters received by registrants in other industries and are covered in the rest of this publication.

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Short-duration disclosures	1	2
Non-GAAP financial measures	2	1
Income taxes	3	4
Revenue recognition	4	**
Internal control over financial reporting	5	5

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to registrants about Forms 10-K from 1 July 2016 through 30 June 2018. In some cases, individual SEC staff comments are assigned to multiple topics if the same comment covers multiple accounting or disclosure areas.

\*\* This topic was not among the top five in 2017.

This supplement should be read in conjunction with the topics in the main section of this publication.

In its comments, the SEC staff may request additional information about a topic and compliance with SEC rules or accounting literature. However, the SEC staff comments are based on the registrant's facts and circumstances, including judgments about materiality. This supplement can help companies identify the SEC staff's areas of focus, but registrants should also consider the significance of the disclosures to investors when including the disclosures in their filings.

### Short-duration disclosures

#### *Summary of issues noted*

The SEC staff continues to ask insurance registrants questions to further understand their disclosures about short-duration contracts under ASC 944, *Financial Services – Insurance*.

#### *Analysis of current issues*

Insurance registrants with short-duration insurance contracts adopted revised disclosure requirements during the 2016 financial reporting cycle. The SEC staff has asked insurance registrants to further explain how their disclosures comply with the guidance and meet the overall objectives of increasing the decision usefulness of the information about a reporting entity's insurance liabilities and improving the comparability between reporting entities.

The SEC staff's questions have focused on understanding the registrant's level of disaggregation and how loss reserve development in the required tables correlates to both the aggregate rollforward of loss reserves and the discussion in the MD&A. The SEC staff has also questioned whether registrants are adequately disclosing claim frequency and incurred-but-not-reported methodologies and properly labeling required supplementary information.

## Life sciences supplement

In this supplement, we analyze trends in SEC staff comment letters to registrants in the life sciences industry. The following table summarizes the topics the SEC staff focused on most often in comment letters sent to life science registrants. Many of these topics are frequent areas of comment in letters received by registrants in other industries and are covered in the rest of this publication.

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Management's discussion and analysis	1	1
Revenue recognition	2	3
Research and development expenses	3	**
Fair value measurements***	4	5
Liabilities, payables and accrual estimates	5	**

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to registrants about Forms 10-K from 1 July 2016 through 30 June 2018. In some cases, individual SEC staff comments are assigned to multiple topics if the same comment covers multiple accounting or disclosure areas.

\*\* This topic was not among the top five comment areas in 2017.

\*\*\* This category includes SEC staff comments on fair value measurements under ASC 820 as well as fair value estimates, such as those related to revenue recognition, stock compensation and goodwill impairment analyses.

This supplement should be read in conjunction with the topics in the main section of this publication.

In its comments, the SEC staff may request additional information about a topic and compliance with SEC rules or accounting literature. However, the SEC staff comments are based on the registrant's facts and circumstances, including judgments about materiality. This supplement can help companies identify the SEC staff's areas of focus, but registrants should also consider the significance of any disclosures to investors when including the disclosures in their filings.

### Research and development expenses

#### *Summary of issues noted*

The SEC staff has asked life sciences registrants to expand disclosures about research and development (R&D) costs by project and by type of cost.

#### *Analysis of current issues*

Life sciences registrants incur significant R&D costs to develop the product candidates in their pipeline. These costs often include a combination of internal (e.g., salaries and related expenses for personnel, laboratory equipment and supplies) and external (i.e., payments to contract research organizations and contract manufacturers) expenditures.

ASC 730-20-50 requires registrants to disclose the costs incurred under significant R&D arrangements but permits those disclosures to be aggregated by type of arrangement. Generally, registrants with multiple product candidates have a variety of R&D arrangements. As a result, the SEC staff may request that life sciences registrants provide further details about R&D arrangements and costs by project for each period presented. In addition, the SEC staff has requested that registrants provide disclosures of R&D costs that are not directly attributable to individual projects by type (e.g., facility depreciation, stock-based compensation, R&D support services).

**Example SEC staff comment: Research and development expenses**

As required by ASC 730-20-50-1, please provide us a schedule by type and amounts of costs incurred included in research and development expenses for each significant agreement.

## Oil and gas supplement

In this supplement, we analyze trends in SEC staff comment letters to registrants in the oil and gas industry. The following table summarizes the topics the SEC staff focused on most often in comment letters sent to registrants in the oil and gas industry. Many of these topics are frequent areas of comment in letters received by registrants in other industries and are covered in the rest of this publication.

Comment Area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Oil and gas reserves	1	3
Management's discussion and analysis	2	2
Non-GAAP financial measures	3	1
Fair value measurements***	4	4
Inventory and cost of sales	5	**

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to registrants about Forms 10-K from 1 July 2016 through 30 June 2018. In some cases, individual SEC staff comments are assigned to multiple topics if the same comment covers multiple accounting or disclosure areas.

\*\* This topic was not among the top five comment areas in 2017.

\*\*\* This category includes SEC staff comments on fair value measurements under ASC 820 as well as fair value estimates, such as those related to revenue recognition, stock compensation and goodwill impairment analyses.

This supplement should be read in conjunction with the topics in the main section of this publication.

In its comments, the SEC staff may request additional information about a topic and compliance with SEC rules or accounting literature. However, the SEC staff comments are based on the registrant's facts and circumstances, including judgments about materiality. This supplement can help companies identify the SEC staff's areas of focus, but registrants should also consider the significance of the disclosures to investors when including the disclosures in their filings.

### Oil and gas reserves

#### **Summary of issues noted**

Registrants are required to disclose a significant amount of information about their oil and gas reserves under ASC 932-235 and Regulations S-X and S-K. In addition to the areas discussed below, the SEC staff continues to monitor consistency between a registrant's reserve disclosures in the supplemental information accompanying its financial statements and:

- ▶ Information in MD&A
- ▶ Prior filings (e.g., the prior-year annual report)
- ▶ Other publicly available information (e.g., information on its website, information discussed in earnings calls)
- ▶ Market data (e.g., market prices)

The SEC staff has also requested additional information to support reserve amounts, including well information, income forecasts, engineering reports, maps and other documentation. The SEC staff inquires about how information that may be relevant to the recognition of oil and gas reserves is evaluated by management. This information may include current and expected market prices, development costs and other estimates that may be relevant to the recognition of oil and gas reserves.

### *Recognition of proved undeveloped reserves (PUDs)*

To recognize PUDs, a registrant must have made a final investment decision to develop an oil and gas property within five years of initial disclosure, with limited exceptions. To meet this criterion, the registrant must be able to demonstrate, with reasonable certainty, that it will execute the development plan within the five-year period. The SEC staff expects development plans to include management's expectations about capital expenditures and related financing. If the registrant changes its development plan, the SEC staff may question whether the registrant had reached a final investment decision.

The SEC staff may request historical information, such as rollforwards of PUD properties, to evaluate how closely the registrant's drilling activities on specific properties align with its plans for those properties. A registrant that cites a significant change in prices to explain a change in its development plan may receive questions from the SEC staff about whether it has identified the appropriate period to recognize PUDs. If planned drilling has not occurred, the staff may challenge whether the registrant appropriately recognized PUDs in the past and whether the registrant should continue to do so.

#### **Example SEC staff comment: Final investment decision**

Please provide us with your development schedule, indicating for each future period, the net quantities of proved reserves and estimated capital expenditures necessary to convert all of the proved undeveloped reserves disclosed as of December 31, 2016, to be developed. Please refer to Rule 4-10(a)(31)(ii) of Regulation S-X and Question 131.04 in the Compliance and Disclosure Interpretations, and either confirm or tell us the extent to which all of the proved undeveloped locations are part of a development plan that has been adopted by your management, including approval by your Board of Directors, if such approval is required, and is current as of December 31, 2016. Include details specifying the steps you have taken to demonstrate more than the mere intent to develop these PUDs.

### *Routine evaluation of PUD classification*

The SEC staff often requests that the registrants that revise their PUD reserves describe the procedures and controls they have in place to evaluate the appropriateness of PUD classification. Additionally, the SEC staff requests clarification regarding any instances in the last five years when PUDs were not converted to proved developed reserves.

#### **Example SEC staff comment: Routine evaluation of PUD classification**

Describe the steps routinely taken to evaluate interim and annual changes in your development schedule to determine whether your PUDs continue to meet the requirements for disclosure. In addition, tell us about any instances in the last five fiscal years where drilling activity was deferred from the original drilling schedule and PUDs were not converted to proved developed reserves within their five-year life.

The SEC staff has asked registrants to expand disclosures about the cost of developing PUDs.

#### *Conversion of PUDs*

The SEC staff requests that registrants with a large percentage of proved reserves classified as PUDs provide additional information about the amount and percentage of PUDs that were converted to developed reserves over the past several years. When the average historical conversion rates are less than 20%, the SEC staff may challenge whether the registrant will be able to execute plans to develop PUDs within the five-year guideline. The SEC staff also may request that registrants expand their disclosures about factors that affected historic conversion rates and their current expectations about the development plan for PUDs.

#### **Example SEC staff comment: PUD conversion**

You disclose that you converted approximately 10% of the PUD reserves available at year-end 2016 to developed status. In part, the Glossary of FASB ASC Section 932-235-20 limits “Proved Undeveloped Oil and Gas Reserves” as follows, “Undrilled locations can be classified as having undeveloped reserves only if a development plan has been adopted indicating that they are scheduled to be drilled within five years, unless the specific circumstances justify a longer time.” Given that your rate of development, if sustained, would not be sufficient to develop your reserves over the next five years, disclose the reasons for the limited progress made during 2016 and explain how your plans relating to the conversion of your remaining proved undeveloped reserves have changed to ensure that your reserve estimates adhere to the criteria in Rule 4-10(a)(31)(ii) of Regulation S-X. Please note, disclosure under Item 1203(c) of Regulation S-K should inform readers regarding progress, or lack thereof, and any factors that affected progress in converting proved undeveloped reserves to developed status.

The SEC staff has asked registrants to expand disclosures about the cost to develop PUDs. Additionally, the SEC staff has inquired about the effects of expected reductions in capital spending on PUD development plans or challenged expected development cost assumptions in the standardized measure of discounted future net cash flows when these assumptions deviate significantly from historic results.

#### **Example SEC staff comments: PUD conversion costs**

We note that you disclosed that in preparing your 2016 capital expenditure budget of approximately \$50 million, you had assumed there would be an improvement in commodity prices by the summer of 2016, although you also indicate that if commodity prices stayed at current levels or declined further, your capital expenditure budget could be reduced to approximately \$20 million. You also disclose that substantially all of the \$20 million would be spent on completing previously drilled wells in the XYZ Field in the ABC region and that these wells were classified as proved developed non-producing as of December 31, 2016. Please tell us and expand your disclosure to explain how your development plan schedules comply with the timeframe stipulated in Rule 4-10(a)(31)(ii) of Regulation S-X, regarding the proved undeveloped reserves that you have disclosed as of December 31, 2016.

### *Explanation of changes in PUD reserves*

Item 1203(b) of Regulation S-K requires disclosures about material changes in PUD reserves. The SEC staff frequently asks registrants to expand their disclosures relating to the nature of changes to PUD reserves to include all relevant factors that affected the change in PUDs, including offsetting amounts.

#### **Example SEC staff comment: Explanation of changes in PUDs**

Please expand your disclosure to provide an explanation for the material changes in the net quantities of your proved undeveloped reserves that occurred during the year. Your disclosure should reconcile the overall change for the line item by separately identifying and quantifying each factor, including any offsetting factors, that contributed to a material change in your proved undeveloped reserves so that the change in net reserves between periods is fully explained. For example, for revisions in previous estimates, identify such factors as changes caused by commodity prices, well performance, uneconomic proved undeveloped locations or the removal of proved undeveloped locations due to changes in a previously adopted development plan. Refer to Item 1203(b) of Regulation S-K.

### *Expiring acreage*

Item 1208(b) of Regulation S-K requires disclosures under appropriate captions in SEC filings about undeveloped acreage, both leases and concessions, including, if material, the minimum remaining terms of leases and concessions. When a registrant has a significant number of lease expirations in the near term, the SEC staff frequently asks whether there are significant PUD reserves associated with those properties and whether they will be developed prior to lease expiration.

#### **Example SEC staff comment: PUDs and expiring acreage**

You disclose that leases for 25% of your undeveloped acreage will expire in 2016. Please tell us the extent to which your proved undeveloped reserves are attributed to acreage having expiration dates that precede the scheduled date for initial development, and explain how you expect to forestall the expiry of such acreage.

### *Presentation of NGLs*

ASC 932-235-50-4(a) requires separate disclosure of natural gas liquids (NGLs) reserves if those volumes are significant. When a registrant refers to NGLs in other portions of a filing but does not separate these volumes for reserve reporting, the SEC staff asks the registrant to address the significance of NGLs.

#### **Example SEC staff comment: Presentation of NGLs**

Explain to us how you have evaluated the significance of your NGL volumes for purposes of reserve reporting. Please note that FASB ASC 932-235-50-4(a) requires separate disclosure for natural gas liquids reserves, when such reserve quantities are significant.

## Real estate supplement

In this supplement, we analyze trends in SEC staff comment letters to registrants in the real estate industry. The following table summarizes the topics the SEC staff focused on most often in comment letters sent to registrants in the real estate industry. Many of these topics are frequent areas of comment in letters received by registrants in other industries and are covered in the rest of this publication.

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Non-GAAP financial measures	1	1
Fair value measurements***	2	2
Consolidation	3	5
Fixed assets (including valuation issues)	4	**
Intangible assets and goodwill	5	**

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to registrants about Forms 10-K from 1 July 2016 through 30 June 2018. In some cases, individual SEC staff comments are assigned to multiple topics if the same comment covers multiple accounting or disclosure areas.

\*\* This topic was not among the top five in 2017.

\*\*\* This category includes SEC staff comments on fair value measurements under ASC 820 as well as other fair value estimates, such as those related to revenue recognition, stock compensation and goodwill impairment analyses.

This supplement should be read in conjunction with the topics in the main section of this publication.

In its comments, the SEC staff may request additional information about a topic and compliance with SEC rules or accounting literature. However, the SEC staff comments are based on the registrant's facts and circumstances, including judgments about materiality. This supplement can help companies identify the SEC staff's areas of focus, but registrants should also consider the significance of the disclosures to investors when including the disclosures in their filings.

### Funds from operations and other non-GAAP financial measures

#### *Summary of issues noted*

The SEC staff often asks registrants to reconcile funds from operations (FFO) and other non-GAAP measures to the most directly comparable US GAAP financial measure. The staff also comments on non-standard adjustments to FFO, challenges the labeling of the resulting non-GAAP measure and questions whether related per-share presentations are in substance impermissible per share liquidity measures.

#### *Analysis of current issues*

Many real estate investment trusts (REITs) disclose FFO, a non-GAAP measure of financial performance that is defined by the National Association of Real Estate Investment Trusts (NAREIT). The SEC staff accepts NAREIT's definition of FFO as a performance measure and will not object to the presentation of FFO per share. The market closely follows REITs' FFO expectations, and investors and analysts view FFO as a key performance indicator.

The SEC staff frequently asks registrants to reconcile FFO and other non-GAAP financial measures to comparable US GAAP measures.

However, some real estate companies provide modified calculations of FFO, such as “adjusted” FFO (AFFO), “modified” FFO and “core” FFO, and they may use different methods to calculate these measures. In some cases, registrants have used entity-specific adjustments that management says are important to investors.

The SEC staff asks management to explain modifications and adjustments to calculations of FFO disclosures. In some cases, registrants are asked to revise or remove adjustments or provide additional information to clarify the purpose of an adjustment. For example, the SEC staff has commented on adjustments for the amortization of certain intangibles, which are inconsistent with the FFO measure as defined by NAREIT.

The SEC staff also has focused on the calculations and presentation of FFO included in a REIT’s earnings release, including forward-looking guidance. The staff frequently has asked entities to reconcile calculations of FFO and other non-GAAP measures in the earnings release to the most directly comparable US GAAP financial measures.

**Example SEC staff comment: Non-GAAP measures – reconciliation**

We note that you provide quarterly and full-year FFO guidance ranges. Given the lack of similar GAAP information and quantitative reconciliation between the GAAP and non-GAAP information, please clarify how your presentation satisfies the requirements outlined within Item 10(e)(1)(i)(A) of Regulation S-K. Reference is also made to Question 102.10 of the updated Compliance and Disclosure Interpretations issued on May 17, 2016.

Real estate registrants should also evaluate any adjustments they make to FFO to make sure that, when they report AFFO per share, they don’t violate Item 10(e) of Regulation S-K that prohibits presenting liquidity measures on a per-share basis. The SEC staff focuses on the substance of a non-GAAP per-share measure rather than management’s characterization of it as a performance measure.

The SEC staff has also focused on making sure that non-GAAP measures are not more prominent than GAAP measures and has asked registrants to re-characterize non-GAAP measures that include unusual adjustments (i.e., adjustments made for items other than interest, taxes, depreciation and amortization in the calculation of EBITDA would require the measure to be labeled “adjusted EBITDA”).

Registrants that present non-GAAP financial measures (e.g., adjusted EBITDA, same-store operating income) are also frequently asked to describe the usefulness of the measure to investors, as required by the SEC’s rules.

### **Example SEC staff comment: Non-GAAP measures**

To provide for ease of understanding the non-GAAP discussion, please consider expanding the first paragraph of this section to name the non-GAAP measures you are presenting (i.e., adjusted income before taxes and related income tax effect, adjusted net income, adjusted diluted earnings per share and EBITDA) and to explain that these measures have been reconciled to the directly comparable GAAP measures as presented in the tables that follow. Also, please define what you consider to be your “core” financial measures or indicate if such measures represent your income before taxes, net income and diluted earnings per share.

Further discussion about SEC comments related to non-GAAP financial measures can be found in the *SEC reporting issues* section of this publication.

### **Resources**

[Technical Line, A closer look at the SEC staff's scrutiny of non-GAAP financial measures](#)  
[2017 SEC annual reports – Form 10-K](#)

## Other industries

The following tables summarize the topics the SEC staff focused on most often in comment letters to registrants in several other industries. Many of these topics are frequent areas of comment in letters received by registrants that are covered in the rest of this publication.

### *Aerospace and defense industry*

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Non-GAAP financial measures	1	**
Management's discussion and analysis	2	1
Revenue recognition	3	**
Segment reporting	4	2
Intangible assets and goodwill	5	**

### *Automotive industry*

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Management's discussion and analysis	1	2
Non-GAAP financial measures	2	1
State sponsors of terrorism	3	**
Income taxes	4	3
Segment reporting	5	**

### *Airlines industry*

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Management's discussion and analysis	1	**
Pension and other post-retirement benefit plans	2	**
Fixed assets (including valuation issues)	3	**
Non-GAAP financial measures	4	1
Depreciation, depletion and amortization	5	**

### *Banking industry*

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Non-GAAP financial measures	1	**
Loans receivables – valuation and allowance	2	1
Acquisitions and business combinations	3	3

**Healthcare industry**

<b>Comment area</b>	<b>Comment rank for the 12 months ended 30 June*</b>	
	<b>2018</b>	<b>2017</b>
Segment reporting	1	3
Non-GAAP financial measures	2	1
Management's discussion and analysis	3	2
Debt, warrants and equity securities	4	**
Fair value measurements***	5	**

**Retail and consumer products industry**

<b>Comment area</b>	<b>Comment rank for the 12 months ended 30 June*</b>	
	<b>2018</b>	<b>2017</b>
Management's discussion and analysis	1	1
Non-GAAP financial measures	2	2
Intangible assets and goodwill	3	**
Fair value measurements***	4	5
Segment reporting	5	3

**Media and entertainment industry**

<b>Comment area</b>	<b>Comment rank for the 12 months ended 30 June*</b>	
	<b>2018</b>	<b>2017</b>
Management's discussion and analysis	1	2
Segment reporting	2	3
State sponsors of terrorism	3	**
Fair value measurements***	4	**
Non-GAAP financial measures	5	1

**Mining and metals industry**

<b>Comment area</b>	<b>Comment rank for the 12 months ended 30 June*</b>	
	<b>2018</b>	<b>2017</b>
Non-GAAP financial measures	1	2
Mining reserves	2	1
Asset sales, disposals, divestures and reorganization issues	3	3
Pro forma financial information	4	**
Fixed assets (including valuation issues)	5	**

**Power and utilities industry**

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Non-GAAP financial measures	1	1
Fair value measurements***	2	2
Fixed assets (including valuation issues)	3	**
Debt, warrants and equity securities	4	**
Internal control over financial reporting	5	**

**Technology industry**

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Management's discussion and analysis	1	2
State sponsors of terrorism	2	3
Non-GAAP financial measures	3	1
Revenue recognition	4	5
Fair value measurements***	5	**

**Telecommunications industry**

Comment area	Comment rank for the 12 months ended 30 June*	
	2018	2017
Non-GAAP financial measures	1	1
Management's discussion and analysis	2	2
Depreciation and amortization	3	5
Internal control over financial reporting	4	**
Leases	5	**

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to registrants about Forms 10-K from 1 July 2016 through 30 June 2018. In some cases, individual SEC staff comments are assigned to multiple topics if the same comment covers multiple accounting or disclosure areas.

\*\* This topic was not among the top five comment areas in 2017.

\*\*\* This category includes SEC staff comments on fair value measurements under ASC 820 as well as fair value estimates, such as those related to revenue recognition, stock compensation and goodwill impairment analyses.

## Appendix B: IPO supplement

This supplement should be read in conjunction with the topics in the main section and industry supplements that may be relevant to a company's IPO registration statement.

The following chart summarizes the 10 most frequent comment areas related to registration statements on Form S-1 in the current and previous years:

Comment area	Comment rank for the 12 months ended 30 June		Comments as % of total registrants that received comment letters*
	2018	2017	2017 and 2018
Management's discussion and analysis	1	1	51%
Risk factors	2	2	56%
Use of proceeds	3	5	36%
Signatures, exhibits and agreements	4	3	39%
Fair value measurements***	5	8	23%
Pro forma financial information	6	6	26%
Executive compensation	7	9	22%
Revenue recognition	8	**	22%
Terms of the offering	9	4	24%
Debt, warrants and equity security issues	10	7	21%

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to companies about Form S-1 IPO registration statements from 1 July 2016 through 30 June 2018. The analysis excludes comments related to the general updating of prospectus information, testing-the-waters communications and related-party transactions.

\*\* This topic was not among the top 10 comment areas in 2017.

\*\*\* This category includes SEC staff comments on fair value measurements under ASC 820 as well as fair value estimates, such as those related to revenue recognition, stock compensation and goodwill impairment analyses.

This supplement excludes SEC staff comments related to several comment areas that are discussed elsewhere in this publication. It discusses specific matters and topics that the SEC staff has raised in comments related to IPO registration statements, including matters related to stock compensation, pro forma financial information and disclosure of intended use of proceeds of the offering.

In its comments, the SEC staff has requested additional information about the topic and compliance with SEC rules or accounting literature. However, the SEC staff comments vary based on facts and circumstances, including judgments about materiality. This supplement can help companies identify the SEC staff's areas of focus, but companies should consider the significance of any disclosures to investors when determining which disclosures to include in their filings.

## Valuation of pre-IPO equity securities

The SEC staff may ask registrants for additional information about their valuation of pre-IPO equity securities issued as compensation.

### *Summary of issues noted*

The SEC staff has continued to ask companies for information to support their valuations underlying share-based payment awards, especially when the fair value of the company's pre-IPO common stock is significantly less than the expected IPO price.

### *Analysis of current issues*

One of the key accounting issues in many IPO transactions is the valuation of equity securities (including stock options) issued as compensation while a company is privately held. In many cases, the estimated fair value of equity securities granted in the months before the IPO is significantly less than the IPO price. As a result, the SEC staff may question pre-IPO fair value estimates that are outside the offering price range and the adequacy of the related disclosures in the financial statements and MD&A.

### **Example SEC staff comment: Valuation of pre-IPO equity securities**

Once you have an estimated offering price or range, please explain to us how you determined the fair value of the common stock underlying your equity issuances and the reasons for any differences between the recent valuations of your common stock leading up to the IPO and the estimated offering price. This information will help facilitate our review of your accounting for equity issuances including stock compensation.

The SEC's FRM states that companies should disclose all of the following information on share-based compensation in the financial statements included in an IPO filing:

- ▶ The methods used to determine the fair value of the company's shares and the material assumptions used in determining the fair value
- ▶ The extent to which such estimates are considered highly complex and subjective
- ▶ That such estimates will not be necessary for new awards once the shares begin trading

Companies should discuss the material assumptions used and describe the methodology and judgments used, highlighting that they may be complex and subjective.

However, the FRM states that, while the SEC staff may issue comments to help it understand unusual valuations, the staff will not expect expanded disclosure in MD&A about the underlying events and business developments that affected such valuations.

The SEC staff expects registrants to support judgments and estimates about the fair value of their securities any time they grant significant share-based payments. The AICPA's Accounting and Valuation Guide, *Valuation of Privately-Held-Company Equity Securities Issued as Compensation* (the Guide), provides a framework and best practices for valuing private company securities. The SEC staff expects privately held companies contemplating IPOs to apply the Guide's valuation guidance when granting share-based payments.

The Guide recommends that private companies obtain contemporaneous valuations from independent valuation specialists to determine the fair value of securities issued as compensation. The SEC staff frequently has asked about estimates of the fair value of share-based payments issued before the IPO, even if a contemporaneous independent valuation has been obtained. Accordingly, a well-documented timeline of significant events (e.g., significant new customer contracts, regulatory approval of products and services), along with contemporaneous valuations supporting grants throughout the 12-month period before an IPO, can help a company support its judgments and assumptions.

The SEC staff expects private companies to consider other relevant data points when valuing equity securities. For example, private companies may sell equity securities to third parties, or employees and other stockholders may sell shares in secondary markets. The SEC staff expects registrants to provide an analysis of the weightings assigned to any stock sales on or before the valuation date.

***EY resources***

*Financial reporting developments, [Share-based payment](#)*

*Best practices when going through the [IPO registration process](#)*

## Pro forma financial information in IPO registration statements

### *Summary of issues noted*

Certain circumstances related to IPOs may warrant the presentation of pro forma financial information on the face of the financial statements included in the IPO registration statement. In these situations, the SEC staff has asked registrants about how they have considered the need to present pro forma information in light of the SEC staff's guidance. The staff also asks whether the pro forma adjustments are appropriate under Article 11 of Regulation S-X.

### *Analysis of current issues*

When IPO proceeds are used to pay dividends to the issuer's prior owners, promoters and/or parents, SAB Topic 1.B.3 requires the issuer to evaluate whether it is required to present pro forma EPS or a pro forma balance sheet on the face of the financial statements included in the IPO filing. Companies should provide a pro forma balance sheet alongside the historical financial statements to reflect an accrual, with an offsetting amount to retained earnings if the dividends are not reflected in the latest balance sheet. In addition, the SAB requires pro forma EPS to be presented if dividends paid at or before the closing of an IPO are greater than the earnings for the most recent year.

The SEC staff has also commented on the application of the SAB when the registrant has paid dividends during the 12 months before the offering or disclosed its intent to pay dividends using IPO proceeds.

#### **Example SEC staff comment: SAB Topic 1.B.3**

We note that as part of your use of the net proceeds from this offering you intend to make a distribution to shareholders. Please explain to us what consideration you gave to providing a pro forma balance sheet alongside your latest historical balance sheet reflecting the distribution accrual (but not giving effect to the full offering proceeds) and providing pro forma earnings per share information giving effect to the number of shares whose proceeds would be necessary to pay the distribution. Reference is made to SAB Topic 1.B.3.

Companies also may be required to present pro forma EPS or a pro forma balance sheet in connection with an IPO when there are material changes in their capital structure or tax status or when IPO proceeds will be used to extinguish debt.

The SEC has provided certain criteria in Article 11 of Regulation S-X for pro forma adjustments that registrants must comply with when preparing pro forma financial information under S-X Article 11. However, it isn't always clear how an issuer should apply the criteria in S-X Article 11 for identifying what constitutes an appropriate pro forma adjustment. The SEC staff, in fact, frequently comments on pro forma adjustments. The staff in the SEC's Division of Corporation Finance also has included some interpretive guidance for certain adjustments in its FRM.

**Example SEC staff comment: Appropriateness of Pro forma adjustments**

We note from pro forma adjustment (C) that you plan to recognize a gain on the forgiveness of interest in the amount of XXX and reduction of debt to XXX that occurred on July 25, 2017. In light of the fact that this is a nonrecurring gain, it should not be included in your pro forma statements of operations.

See guidance in Article 11 of Regulation S-X and revise your pro forma financial information accordingly.

Issuers need to carefully consider the criteria in Article 11 to support each adjustment. They also need to focus on making clear and transparent disclosures about pro forma adjustments.

**EY resources**

[Financial reporting developments, \*Earnings per share\*](#)

[Pro forma financial information – A guide for applying Article 11 of Regulation S-X](#)

[Best practices when going through the IPO registration process](#)

## Use of proceeds

### *Summary of issues noted*

The SEC staff has continued to ask registrants to clearly disclose the principal purposes for which the net proceeds of the offering will be used and the approximate amount they will spend from the net proceeds for each purpose.

### *Analysis of current issues*

Item 504 of Regulation S-K requires registrants to describe their planned uses and amounts of offering proceeds. These disclosures are intended to help users understand whether any proceeds will be used to discharge debts, to complete an acquisition or for working capital, for example. The SEC staff may request that a company provide additional details about how it will use proceeds from the offering, particularly when other disclosures in the filing imply a use omitted from the Item 504 disclosures.

The staff often asks registrants to quantify the proceeds that will be used for each major purpose. For example, when an issuer discloses a broad purpose, the staff may ask the company to be more specific and to quantify the amounts that will be used for each major purpose.

#### **Example SEC staff comment: Quantification of planned uses of proceeds**

We note your disclosure in the third paragraph that you “plan to use the net proceeds [you] will receive from this offering for general corporate purposes in line with [your] strategies.” Please revise to more specifically identify and quantify the principal intended uses of the net proceeds.

#### ***EY resources***

[\*Best practices when going through the IPO registration process\*](#)

## Appendix C: Foreign private issuers

The SEC staff's comments to foreign private issuers (FPIs) that prepare their financial statements in accordance with either US GAAP or IFRS often are similar to its comments to domestic registrants.

Many of the topics in the main section of this publication and industry supplements are relevant for FPIs and therefore are not discussed at length here, such as:

- ▶ MD&A matters, including comments on critical accounting estimates, results of operations and liquidity
- ▶ Consolidation, including variable interest entities
- ▶ Fair value measurements
- ▶ Business combinations
- ▶ Oil and gas reserves
- ▶ Operating items, including revenue recognition, hedging and impairment
- ▶ Segment reporting
- ▶ Intangible assets and goodwill

The following chart summarizes the 10 most frequent comment areas in 2018 and 2017 related to annual reports on Form 20-F:

Comment area	Ranking 12 months ended 30 June		Comments as % of total registrants that received comment letters*
	2018	2017	
Management's discussion and analysis	1	1	37%
State sponsors of terrorism	2	4	27%
Non-GAAP financial measures	3	2	26%
Fair value measurements***	4	3	18%
Revenue recognition	5	10	8%
Oil and gas reserves	6	7	9%
Intangible assets and goodwill	7	8	8%
Acquisitions, mergers and business combinations	8	**	6%
Fixed assets	9	5	10%
Segment reporting	10	6	11%

\* These rankings are based on topics assigned by research firm Audit Analytics for SEC comment letters issued to registrants about Form 20-F from 1 July 2016 through 30 June 2018. In some cases, individual SEC staff comments are assigned to multiple topics if the same comment covers multiple accounting or disclosure areas.

\*\* This topic was not among the top 10 comment areas in 2017.

\*\*\* This category includes SEC staff comments on fair value measurements under ASC 820 and IFRS 13, *Fair Value Measurement*, as well as fair value estimates, such as those related to revenue recognition, stock compensation and goodwill impairment analyses.

Below are unique matters that the SEC staff often raised in comments to FPIs.

## ***Activities with countries designated as state sponsors of terrorism***

### ***Summary of issues noted***

The SEC staff frequently asks FPIs to provide additional information about business activities in or with countries identified by the US State Department as state sponsors of terrorism, which currently are Iran, Sudan, North Korea and Syria. The SEC staff reviews various sources of information, including past filings and correspondence, news articles, company websites and press releases that include company locations and contact information, to identify registrants with operations in these countries. If an FPI has been identified as having any business in or with one of those countries, the SEC staff periodically (e.g., every year or two) asks for updates on those activities.

### ***Analysis of current issues***

US securities laws do not impose a specific disclosure requirement that addresses business activities in or with a country based on its designation as a state sponsor of terrorism. However, Rule 408 of Regulation C and Exchange Act Rule 12b-20 require a registrant to disclose additional information if it is material and necessary to make a company's statements, in light of the circumstances under which they were made, not misleading. Because of these rules, the SEC staff frequently asks registrants to provide the following information and to disclose it if it is material:

- ▶ The nature and extent of past, current and any anticipated operations in or activities with a country designated as a state sponsor of terrorism, whether through subsidiaries, partners, customers, affiliates, joint ventures, distributors, resellers or other direct or indirect arrangements
- ▶ Any services, products, information or technology provided to and agreements, commercial arrangements or other contracts entered with governments or entities controlled by the governments designated as state sponsors of terrorism
- ▶ Whether any of the technologies or materials provided or intended to be provided to a country designated as a state sponsor of terrorism are controlled items included in the US Department of Commerce's Commerce Control List
- ▶ Whether operations in or with state sponsors of terrorism constitute a material risk in quantitative terms by discussing revenues, assets and liabilities associated with such operations and qualitative factors that a reasonable investor would deem important in making an investment decision, including any potential adverse effect on company reputation and share value

In addition to these requests for information, the Iran Threat Reduction and Syria Human Rights Act of 2012 amended the Securities Exchange Act of 1934 to require all issuers, including FPIs, to disclose in their annual and quarterly reports filed with the SEC whether they or their affiliates knowingly engaged in various prohibited activities involving Iran.

**Example SEC staff comment: Activities with countries designated as state sponsors of terrorism**

In the Distributor Network section of your website, you append a map that appears to identify Sudan as one of the countries where you sell your products. Sudan is designated by the U.S. Department of State as a state sponsor of terrorism and is subject to U.S. export controls. You do not provide disclosure about Sudan in your Form 20-F. Please describe to us the nature and extent of any past, current and anticipated business with Sudan, whether through distributors, customers or other direct or indirect arrangements.

**Non-GAAP financial measures****Summary of issues noted**

Non-GAAP financial measures continue to be an area of significant focus of the SEC staff. Since the SEC staff updated its C&DIs on the use of non-GAAP financial measures in May 2016, the staff has challenged FPIs on their compliance with these interpretations.

The SEC staff has questioned whether FPIs that apply IFRS have disclosed financial measures in their filings that are required by their other local accounting and disclosure standards. If they are required, an FPI may present the non-GAAP measures (i.e., non-IFRS for FPIs reporting under IFRS) under an exemption in Item 10(e)(5) without complying with the non-GAAP disclosure requirements in the rest of Item 10(e) of Regulation S-K.

**Analysis of current issues**

When an FPI presents non-GAAP financial measures and it is unclear whether the FPI qualifies for the Item 10(e)(5) exemption, the SEC staff asks the registrant to address the following:

- ▶ Whether the measure is required or permitted by local accounting and disclosure standards
- ▶ The literature that the FPI relied on to conclude that its local accounting and disclosure standards either require or permit disclosing the measure

When a non-GAAP financial measure does not qualify for the exemption under Item 10(e)(5) of Regulation S-K, the SEC staff has asked FPIs whether the measure provides useful information to investors about the entity's financial condition and results. The SEC staff has also questioned FPIs about the appropriateness of the reconciliation to the most directly comparable measure under the accounting framework (i.e., US GAAP or IFRS) the FPI is using.

The SEC staff also evaluates all non-GAAP items, including those expressed as percentages or per-share amounts and questions their labeling if it is inconsistent with the nature of the adjustments to GAAP measures.

**Example SEC staff comment: Reconciliation of non-GAAP measures**

You have asserted that the measures specified are not non-GAAP measures defined by Item 10(e)(2) of Regulation S-K. Instead you believe they are Regulatory Performance Measures. Please tell us whether the measures are required by a regulatory agency. If the measures are not currently required to be disclosed by IFRS, Commission Rules or other regulatory requirements, you should disclose that the measures are non-GAAP measures and comply with Item 10(e) of Regulation S-K. Please refer to Item 10(e)(5) in Regulation S-K and to our updated Compliance and Disclosure Interpretations issued on May 17, 2016, specifically question 102.12.

## Appendix D: SEC review process and best practices

The DCF of the SEC selectively reviews filings made under the Securities Act of 1933 and the Securities Exchange Act of 1934 (Exchange Act) to monitor and enhance compliance with disclosure and accounting requirements. In its filing reviews, DCF accountants concentrate on disclosures and accounting methods that may conflict with US GAAP or SEC rules or that may need clarification. Other DCF staff may review other aspects of SEC filings for compliance with the federal securities laws and regulations. DCF performs its primary review responsibilities through staff in 11 offices that each focus on an industry. The DCF assigns public companies in a particular industry to one of these 11 Assistant Director Offices as shown below based upon their Standard Industrial Classification (SIC) code. Each company's office assignment is listed in EDGAR in the basic company information that precedes the company's filing history.

Office	Primary industries
1	Healthcare and insurance
2	Consumer products
3	Information technologies and services
4	Natural resources
5	Transportation and leisure
6	Manufacturing and construction
7	Financial services
8	Real estate and commodities
9	Beverages, apparel and mining
10	Electronics and machinery
11	Telecommunications

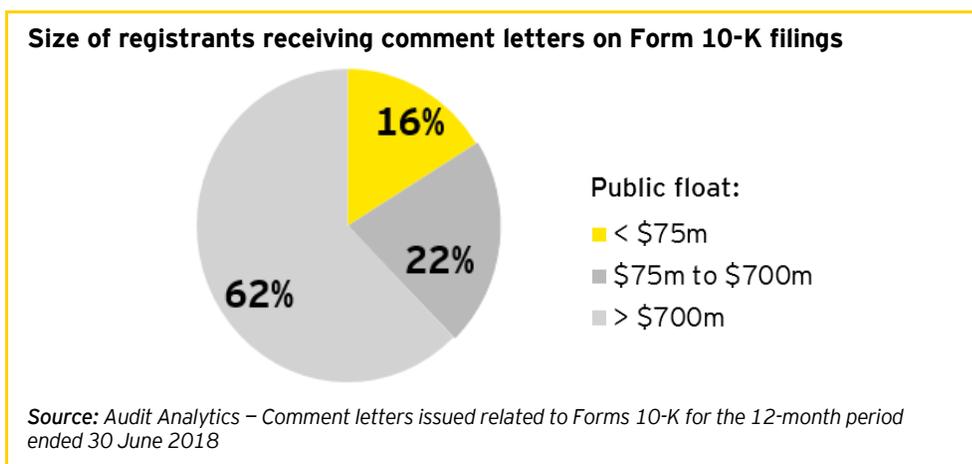
In its filing reviews, DCF staff focuses on disclosures and accounting methods that may conflict with FASB or SEC rules or that need clarification.

The SEC also has a number of legal and accounting technical offices staffed by people who support the filing reviews by focusing on highly technical matters without regard to specific industries. The staff in the assistant director offices consult most often with staff in the Offices of Chief Accountant, Chief Counsel, Mergers and Acquisitions, and International Corporate Finance. The DCF also has a Chief Risk Officer who focuses on internal controls related to the review program to maintain the quality of the staff's filing reviews.

### ***Required and selective review***

As required by the Sarbanes-Oxley Act of 2002, DCF staff reviews, at some level, every registrant at least once every three years, but it reviews many registrants more frequently. In addition, DCF staff generally reviews all IPOs and selectively reviews other transactional filings, such as those made in connection with business combination transactions, proxy statements or other public offerings. The DCF staff sends "no review" letters when it has not selected an issuer's registration statement for review.

The SEC staff has reviewed slightly over 50% of registrants each year since 2013. In addition, the SEC staff has sent the majority of its comment letters to larger public companies, as illustrated below:<sup>4</sup>



#### **Levels of review**

If the DCF staff selects a filing for review, the extent of that review will depend on many factors. The level of review may be:

- ▶ A full cover-to-cover review in which DCF staff examines the entire filing for compliance with the applicable requirements of the federal securities laws and regulations
- ▶ A financial statement review in which DCF staff examines the financial statements and related disclosures, such as MD&A, for compliance with the applicable accounting standards and SEC disclosure requirements
- ▶ A targeted issue review in which DCF staff examines one or more specific items of disclosure in the filing for compliance with the applicable accounting standards or the disclosure requirements of the federal securities laws and regulations

DCF staff may not always inform registrants of the type of review performed (such as a targeted review or a full review), but it will focus on what it considers necessary in the company's circumstances. When DCF staff believes that a registrant can enhance its disclosure or improve its compliance with the applicable disclosure requirements, it provides comments in a letter to the registrant. The range of possible comments is broad and depends on the issues that arise in a particular filing review. The DCF staff completes many filing reviews without issuing any comments. In those cases, the registrant will not be notified that its SEC filing was reviewed.

In addition to an initial reviewer, at least one other more senior DCF staff member typically reviews a filing and proposed comments. This second-level review is intended to enhance quality and consistency across filing reviews.

<sup>4</sup> This graph shows the size (based on public float) of companies that received comment letters on Form 10-K filings during the 12 months ended 30 June 2018. However, the SEC staff may not send a comment letter to every registrant that it reviews.

### ***DCF staff comments***

DCF staff views the comment process as a dialogue with a registrant about its disclosures. DCF staff's comments are in response to a registrant's disclosures and other public information and are based on DCF staff's understanding of that registrant's facts and circumstances.

In its initial comments, DCF staff often requests information so it can better understand the registrant's facts and circumstances. These requests should not be interpreted to mean that the staff has concluded that the disclosures must change. In many cases, comments are resolved once the DCF staff has gained a full understanding of a registrant's facts and circumstances and has obtained sufficient insight into the judgments made by management that led to the disclosures. Registrants may commit to modifying their disclosure in the future in order to resolve certain comments. The DCF staff rarely requires a registrant to amend a filing unless the staff's comment relates to a transactional filing such as an IPO or results in a material restatement to the financial statements.

### ***Best practices for registrant responses to comments***

A registrant generally responds to an SEC comment letter by sending a letter back to DCF staff. When responding to DCF staff comment letters, registrants should consider the following:

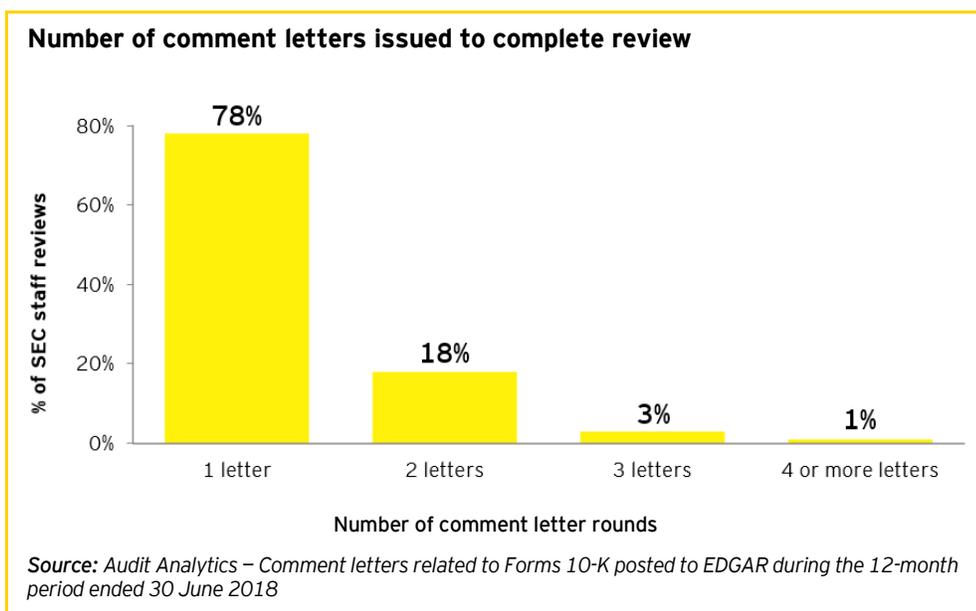
- ▶ Registrants should assume that DCF staff has not yet concluded on a matter and merely needs more information, unless the staff clearly indicates in its comment this is not the case.
- ▶ Responses to each comment should focus on the question(s) asked by the SEC staff, and those responses should cite authoritative literature wherever possible.
- ▶ Responses should address the registrant's unique facts and circumstances and provide insight into any judgments made. While it may be helpful to consider responses from other registrants on similar topics, registrants should not copy those responses.
- ▶ Registrants should file all response letters on EDGAR redacting any specific information for which they are seeking confidential treatment.
- ▶ If revisions are being made to a filing as a result of a comment from DCF staff, responses should indicate specifically where these revisions are being made. If disclosure will be modified in a future filing, it can be helpful for the registrant to provide proposed language in its response letter. Registrants should make it clear that facts and circumstances may change in a way that could require disclosure different than that proposed.
- ▶ Companies should seek the input of all appropriate internal personnel and professional advisers (such as legal counsel and independent auditors) so that they fully respond to the comment letter in a complete and accurate manner. Waiting for a later round of comments to involve the necessary resources may delay or hinder a successful resolution.

Proactive communication with DCF staff may expedite the comment letter process.

Providing a thorough explanation or analysis of an issue to DCF staff may help DCF staff better understand the accounting and disclosure, and it often will resolve the comment. To facilitate such responses, registrants should maintain contemporaneous documentation of significant accounting and disclosure decisions. Contemporaneous documentation that already exists is more persuasive than a retrospective defense following receipt of a DCF staff comment.

Depending on the nature of the issue, DCF staff's concerns and the registrant's response, DCF staff may issue more comments following its review of the registrant's response. This comment and response process continues until the DCF staff and the registrant resolve all comments.

The following graph shows the number of comment letters (or rounds) that were issued by the SEC staff for reviews completed during the 12 months ended 30 June 2018:



A substantial majority of reviews are closed after one comment letter, and nearly all are resolved after two letters.

Comment letters from the DCF staff on certain filings often request a written response in 10 business days. If a registrant needs more time to respond, it should contact the DCF staff, which is generally accommodating in granting extensions that will enhance the quality of the response letter. A registrant also may consider contacting the DCF staff if it needs clarification about a comment or informal feedback regarding its approach to responding.

#### ***Closing a filing review***

When a registrant has satisfactorily resolved all DCF staff's comments on a filing, DCF staff provides the registrant with a "completion of review letter" to confirm that the SEC staff's review is complete. To increase the transparency of the review process, after the DCF staff completes a filing review, it publicly releases its comment letters and registrant responses to those letters on the SEC's EDGAR system no earlier than 20 business days after the review's completion.

### ***Reconsideration process***

DCF staff and the registrant may ultimately disagree about an accounting or disclosure matter. A registrant should, in any instance it wishes, seek reconsideration of a comment by other SEC staff, including those in DCF's Office of the Chief Accountant (DCF-OCA).

DCF staff members, at all levels, are available to discuss disclosure and financial statement presentation matters with a registrant and its legal, accounting and other advisers. A registrant may request that more senior DCF staff reconsider a comment or reconsider a DCF staff member's view of the registrant's response at any point in the filing review process. DCF does not have a formal protocol for registrants to follow when seeking reconsideration; a request for reconsideration may be oral or written.

Registrants also may ask the SEC's Office of the Chief Accountant (OCA), which is distinct from the DCF-OCA, to reconsider an accounting conclusion of the DCF staff at any stage in the process. Generally, the SEC's OCA addresses questions about the application of accounting principles while DCF resolves matters concerning the age, form and content of financial statements required to be included in a filing. Even before a registrant requests reconsideration, DCF staff may have consulted internally about the issue with DCF-OCA and then with OCA.

A registrant should initiate a reconsideration with OCA by informing the staff in DCF of its intention to request such reconsideration. In these circumstances, a registrant does not need to make a submission directly to OCA if all of the relevant information is contained in comment letter responses from the registrant to DCF, although a separate submission to OCA may serve to expedite the process.

### ***Disclosure requirements***

The SEC requires that all entities defined as an accelerated filer, a large accelerated filer or a well-known seasoned issuer disclose, in their annual reports on Form 10-K or Form 20-F, written comments DCF staff has made in connection with a review of Exchange Act reports that:

- ▶ The registrant believes are material
- ▶ Were issued more than 180 days before the end of the fiscal year covered by the annual report
- ▶ Remain unresolved as of the date of the filing of the Form 10-K or Form 20-F

The disclosure must identify the substance of the unresolved comments. DCF staff comments that have been resolved, including those that DCF staff and the registrant have agreed will be addressed in future Exchange Act reports, do not need to be disclosed. Registrants can provide other information, including their positions regarding any such unresolved comments. This information is not required in the registrant's quarterly reports on Form 10-Q.

### ***Requests for waivers, pre-clearance and interpretive guidance***

In line with their efforts to promote capital formation, SEC officials are actively encouraging companies to use Rule 3-13 of Regulation S-X to request relief from burdensome financial statement requirements that result in the disclosure of information that exceeds what is material to investors. The DCF staff may use its authority under Rule 3-13 to modify or waive a company's financial reporting obligations under Regulation S-X, based on the facts and circumstances, as long as modifying or omitting the disclosure is consistent with investor protection.

Companies should consider discussing any matters they believe have merit with the staff before drafting a written request for relief under Rule 3-13. Conversations with the staff can be especially valuable when a company has a novel or complex fact pattern. In these situations, a company can learn which points will be most relevant to the staff's evaluation. To make it easier for companies to reach the right person, the SEC staff has updated its FRM<sup>5</sup> to include the names of staff members and the topics on which they answer questions.

Registrants also may request informal interpretive guidance from DCF staff on a named or no-named basis in a telephone call to DCF staff or in a request form for interpretive guidance and other assistance on the SEC's website. Requests made by telephone or an online request form<sup>6</sup> are informal and may remain anonymous; therefore, responses to such requests cannot be relied upon as formal positions of the DCF staff.

In addition, companies may pre-clear conclusions on the application of US GAAP (or IFRS) with the SEC's OCA. OCA staff encourages companies to consult on a pre-filing basis when companies are uncertain about accounting issues. Further discussion of the procedures for consulting with OCA is on the SEC's website at <http://www.sec.gov/info/accountants/ocasubguidance.htm>.

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<sup>5</sup> DCF Financial Reporting Manual at: <https://www.sec.gov/divisions/corpfin/cffinancialreportingmanual.pdf>.

<sup>6</sup> The online request form is available at: [https://tts.sec.gov/cgi-bin/corp\\_fin\\_interpretive](https://tts.sec.gov/cgi-bin/corp_fin_interpretive).

## Appendix E: Abbreviations

Abbreviation	FASB Accounting Standards Codification
ASC 210	FASB ASC Topic 210, <i>Balance Sheet</i>
ASC 250	FASB ASC Topic 250, <i>Accounting Changes and Error Corrections</i>
ASC 260	FASB ASC Topic 260, <i>Earnings Per Share</i>
ASC 280	FASB ASC Topic 280, <i>Segment Reporting</i>
ASC 310	FASB ASC Topic 310, <i>Receivables</i>
ASC 350	FASB ASC Topic 350, <i>Intangibles – Goodwill and Other</i>
ASC 350-20	FASB ASC Topic 350-20, <i>Intangibles – Goodwill and Other – Goodwill</i>
ASC 450	FASB ASC Topic 450, <i>Contingencies</i>
ASC 470	FASB ASC Topic 470, <i>Debt</i>
ASC 480	FASB ASC Topic 480, <i>Distinguishing Liabilities from Equity</i>
ASC 606	FASB ASC Topic 606, <i>Revenue from Contracts with Customers</i>
ASC 740	FASB ASC Topic 740, <i>Income Taxes</i>
ASC 805	FASB ASC Topic 805, <i>Business Combinations</i>
ASC 810	FASB ASC Topic 810, <i>Consolidation</i>
ASC 820	FASB ASC Topic 820, <i>Fair Value Measurement</i>
ASC 842	FASB ASC Topic 842, <i>Leases</i>
ASC 932	FASB ASC Topic 932, <i>Extractive Activities – Oil and Gas</i>
ASC 932-235	FASB ASC Topic 932-235, <i>Extractive Activities – Oil and Gas – Notes to Financial Statements</i>
ASC 944	FASB ASC Topic 944, <i>Financial Services – Insurance</i>
SAB Topic 1.B.3	SEC Staff Accounting Bulletin Topic 1.B.3, <i>Financial Statements, Allocation Of Expenses And Related Disclosure In Financial Statements Of Subsidiaries, Divisions Or Lesser Business Components Of Another Entity, Other Matters</i>
SAB Topic 1.M	SEC Staff Accounting Bulletin Topic 1.M, <i>Financial Statements, Materiality</i>
SAB Topic 1.N	SEC Staff Accounting Bulletin Topic 1.N, <i>Financial Statements, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements</i>
SAB Topic 11.M	SEC Staff Accounting Bulletin Topic 11.M, <i>Miscellaneous Disclosure, Disclosure Of The Impact That Recently Issued Accounting Standards Will Have On The Financial Statements Of The Registrant When Adopted In A Future Period</i>
SAB Topic 14.D.1	SEC Staff Accounting Bulletin Topic 14.D.1, <i>Share-Based Payment, Certain Assumptions Used in Valuation Methods, Expected Volatility</i>
SAB Topic 14.D.2	SEC Staff Accounting Bulletin Topic 14.D.2, <i>Share-Based Payment, Certain Assumptions Used in Valuation Methods, Expected Term</i>
SAB Topic 14.F	SEC Staff Accounting Bulletin Topic 14.F, <i>Share-Based Payment, Classification of Compensation Expense Associated with Share-Based Payment Arrangements</i>
SAB 118	SEC Staff Accounting Bulletin Topic 118, <i>Income Tax Accounting Implications of the Tax Cuts and Jobs Act</i>



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SCORE No. 04321-181US

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