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Snapshot

CAQ issues Sept. SEC Regs Committee highlights

The Center for Audit Quality (CAQ) recently issued highlights of the Sept. 24, 2019, joint meeting between its SEC Regulations Committee and the SEC staff. The SEC Regulations Committee meets periodically with the SEC staff to discuss emerging financial reporting issues relating to SEC rules and regulations. Key topics discussed at the meeting are summarized here.

Non-GAAP financial measures

The SEC staff and committee members continued their ongoing discussion of non-GAAP financial measures, with the staff noting that:

- Disclosures containing non-GAAP margins are only acceptable if, depending on the facts and circumstances, they are reconciled to "gross margin," as defined in GAAP, regardless of whether gross margin is separately presented in the financial statements.
- Registrants should not remove the impact of the adoption of the credit losses standard from a non-GAAP performance measure and may contact the staff to discuss an acceptable approach for presenting the impact of the adoption.
- There should be internal controls surrounding the non-GAAP reporting process, including engagement from audit committees.

Impact of the new leases standard on the contractual obligations table

The SEC staff and committee members discussed the impact of adopting the new leases standard on the contractual obligations table given the accounting differences between the new standard and legacy U.S. GAAP. The staff indicated that they would not expect the change in lease accounting to alter the historical practice that the cash outflows in the contractual obligations table would be consistent with the U.S. GAAP disclosure. The staff further noted that if the amounts do not adequately capture liquidity needs and expected future cash outflows, registrants should assess the need for additional disclosures in the footnotes to the contractual obligations table.

Impact of a retrospective accounting change on selected financial data

Committee members asked the SEC staff how the removal of Financial Reporting Manual (FRM) Section 1610 impacts the historical view to recast years four and five of the selected financial data table upon a retrospective accounting change (other than one related to the adoption of ASC 606). The staff referred to the guidance in Regulation S-K, Item 301, and indicated that registrants may need to exercise judgment in determining whether years four and five need to be recast or whether additional disclosures explaining the material factors affecting the comparability of the information are sufficient.

SPAC's use of pro forma financial information to measure significance

FRM Section 2025.3 permits the use of pro forma information to measure significance for financial statements that are required of a subsequent acquisition under Regulation S-X, Rule 3-05. Despite the guidance in FRM Section 2025.9, which requires a shell company that acquires its predecessor to measure the significance of a second acquisition that occurred in the same year against the registrant's prior-year stand-alone financial statements, committee members asked the SEC staff if a special-purpose acquisition company (SPAC) could apply the accommodations in Section 2025.3. The staff indicated that Section 2025.9 would continue to apply in this fact pattern. Registrants may consult with the staff and request relief under Regulation S-X, Rule 3-13, when they believe the information required by Rule 3-05 is not material to investors.

Impact on Article 11 conclusions on MLP drop-down transactions

Under legacy U.S. GAAP, master limited partnership (MLP) drop-down transactions were accounted for by the MLP as a common control acquisition and concurrent operating lease. These transactions, if significant, historically triggered the need to report the acquisition on Form 8-K, Item 2.01, and to assess the requirements as to whether a business was acquired for reporting purposes under Regulation S-X, Article 11. With the adoption of the new leases standard, these transactions may instead be accounted for as a failed sale-leaseback transaction. The SEC staff stated that they believe these acquisition transactions continue to be within the scope of Form 8-K, Item 2.01, notwithstanding the change in accounting under the new leases standard. Registrants are also encouraged to contact the staff when warranted by their specific facts and circumstances.

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Subsequent to the meeting, the SEC staff made public statements regarding certain of these topics at the 2019 AICPA Conference on Current SEC and PCAOB Developments. For more information, see our *New Developments Summary*, "Highlights of the 2019 AICPA Conference on Current SEC and PCAOB Developments."

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