

## SEC FLASH REPORT

### SEC's Advisory Committee on Improvements to Financial Reporting Releases Final Report

August 4, 2008

On August 1, 2008, the Securities and Exchange Commission (SEC) received the final report of the SEC Advisory Committee on Improvements to Financial Reporting. The report contains 25 recommendations to make financial information more useful and understandable to investors. As promised in our Flash Report dated July 14, 2008, we are issuing this Flash Report to summarize the final recommendations in more detail.

The Advisory Committee, chartered by the SEC in July of 2007, is comprised of a diverse group, such as chief financial officers, external audit firm executives, former regulators, audit committee members as well as investors and other key constituencies in America's capital markets. The SEC asked the Advisory Committee for recommendations on reducing unnecessary complexity in the U.S. financial reporting system and making financial reports clearer and more understandable to investors. The report contains recommendations that can be considered and implemented by the SEC, the Financial Accounting Standards Board (FASB) and the Public Company Accounting Oversight Board (PCAOB).

The scope of the report is limited to matters related to SEC registrants and is organized into four chapters:

- Chapter 1 addresses issues around substantive complexity
- Chapter 2 focuses on the standard-setting process
- Chapter 3 provides recommendations for improving the audit process and compliance
- Chapter 4 suggests ways to improve the delivery of financial information.

The report contains detailed recommendations covering five areas:

- (1) Increasing the usefulness of information in SEC filings, while minimizing burdens on preparers – Among other things, the Committee noted that many individual investors find company filings with the SEC to be overly complex and detailed. The report recommended the inclusion of a short executive summary at the beginning of a company's annual report that would describe concisely the principal components or fundamental drivers of its business and its key performance metrics.
- (2) Enhancing the accounting standards-setting process to make it more effective and efficient – The Committee called for more investor participation in accounting standard setting by increasing investor representation on the FASB and Financial Accounting Foundation (FAF).
- (3) Improving the substantive design of new accounting standards by better articulating the underlying objectives and principles, avoiding all-or-nothing bright-line tests, and moving

away from industry-specific guidance to a focus on the underlying business activity – The Committee noted that the underlying objectives of certain accounting standards are sometimes obscured by dense language, detailed rules, and numerous exemptions. The Committee recommended a different approach to the substantive design of standards. For example, the Committee called for improved rules on off-balance sheet accounting and fewer situations where alternative accounting standards exist for the same transaction. The Committee recommended that companies provide better disclosure to investors about what portion of their earnings constitutes cash or accrued income based on historical cost accounting and what portion represents unrealized gains or losses based on fair value estimates.

- (4) Delineating authoritative interpretive guidance from the non-authoritative literature – To reduce the proliferation of U.S. GAAP, the Committee said it strongly supports the FASB's efforts to complete the codification of all authoritative accounting literature into one document. The Committee said that others, such as external audit firms, may still publish their views on accounting issues; however, those views should be labeled as non-authoritative. In addition, the Committee also called for a clearer delineation of functions on interpreting accounting standards – with the FASB taking the lead on broad issues and the SEC focused on registrant-specific issues.
- (5) Clarifying guidance on financial restatements and accounting judgments – The Committee recommended increased correction of accounting errors and more disclosures about those corrections to investors. However, the Committee asserted that the correction of every accounting error should not automatically result in a restatement of prior year financial statements. The Committee said that in the "dark period" during restatement efforts when companies generally cease filing current financial reports (as they often engage in time consuming and costly projects to finalize the restated financials), companies usually do not provide investors with much information. Therefore, the Committee said it believes that restatements of prior years should only be undertaken for the correction of accounting errors that are material to current investors.

In summary, the objective is to provide clearer guidelines, provide for fewer exceptions to general standards and rules, and create greater focus on what really matters.

The SEC's press release is available at: <http://www.sec.gov/news/press/2008/2008-166.htm>. In it, SEC Chairman Christopher Cox is quoted as stating he has asked the Commission staff to immediately begin analyzing the recommendations, and to prepare regulatory actions based on them wherever appropriate. The press release reports that the Commission already has taken steps to benefit investors based on two earlier recommendations made by the Advisory Committee.

- On May 14, the Commission formally proposed using new technology to get important information to investors faster, more reliably, and at a lower cost by requiring all U.S. companies to provide financial information using interactive data beginning as early as next year. See the SEC press release at <http://www.sec.gov/news/press/2008/2008-85.htm>.
- On July 30, the SEC approved new guidance to public companies to address their concerns about how to comply with the securities laws while developing their Web sites to serve as an effective means for disseminating important information to investors. See SEC Flash Report

dated August 1, 2008. For more information on this recent action, see the SEC press release at <http://www.sec.gov/news/press/2008/2008-158.htm>.

The final report is available through the aforementioned press release and through the Advisory Committee's home page on the SEC site at <http://sec.gov/about/offices/oca/acifr.shtml>. Each chapter's issues and recommendations are summarized in the attached Appendix. The 172 page final report contains considerably more discussion and background related to the recommendations for those who would like additional information regarding the Committee's recommendations and the supporting rationale.

Both the FASB Chairman Robert Herz and PCAOB Chairman Mark Olson have committed to continue working with the SEC to increase the usefulness of the financial reporting system. In making his call for the Commission staff to immediately begin analyzing these recommendations and to prepare appropriate regulatory actions based on them, Chairman Cox did not specify any timetable.

In summary, the Advisory Committee has proposed important recommendations which, if adopted, would have a significant impact on the regulatory and standards setting landscape driving financial reporting practices and quality. Ten key message points around these recommendations are provided below:

- (1) **Put it all in one place:** There is potential for addition or substitution of a new primary financial statement which focuses on and presents operating and cash flow information that provides the "roadmap for valuation." In other words, the information used by analysts, financial buyers and others to value companies would be highlighted in one place.
- (2) **Say it well – but say it once:** There is potential for elimination of redundant disclosures, such as those that currently exist in many SEC filings in areas such as summary data, critical accounting policies, litigation and contingencies, financial commitments, properties owned or leased, etc. There is repetition between the "forepart" and the "F pages" which has been said by some to be principally of benefit only to typesetters and printers. That redundancy would be eliminated.
- (3) **But don't say it forever:** There is potential for ongoing review and *elimination* of disclosures when they are no longer needed. This change would remove what many currently characterize as "cumulative disclosure."
- (4) **Open the tent on standard-setting:** There is potential for admitting "outsiders" such as investors and other financial statement users to the standard-setting process. This change would open the process to enable these parties to exercise both "voice" and "vote" beyond the current participants.
- (5) **Move the meter on global alignment:** There is potential for more "economic view" accounting in such areas as proportional measurement, along with the potential elimination of much of the current industry guidance (including the myriad of exceptions existing in practice). This change would move U.S. financial reporting even closer to alignment with the increasingly globally used international financial reporting standards (IFRS). It is reasonable to expect that the recommendations that facilitate convergence toward IFRS will be factored into the SEC's forthcoming IFRS roadmap.

- (6) **“I know you said ‘it’s not GAAP’ – but everyone knows that it is”:** There is potential for significant limitations on the type and kind of guidance that the SEC staff should give and broadly apply – either in response to trends or to specific questions. This means that there would be an end to “SEC staff speech GAAP” and “SEC comment letter GAAP”, both of which are (regardless of official hierarchy) viewed, in practice, as equivalent to GAAP by companies and their external auditors.
- (7) **To restate or not to restate – that is the question:** There is the potential for consideration of *not* restating as often as is currently the case, while on the other hand, fixing ALL errors when detected regardless of whether a restatement is necessary. This change means that there would be “zero tolerance for errors” coupled with “not always having to revisit prior annual or interim periods.” If the new guidance takes the shape envisioned by the Advisory Committee, it has the potential to bring a sense of perspective and sanity to the financial restatement process.
- (8) **And when the answer is “yes”:** There is potential for guidance to companies engaged in a restatement effort on what to disclose and when and how to disclose it. This guidance would be intended to minimize “dark periods” by addressing how to stay “current” while the company “catches up.”
- (9) **But tell us what really matters:** There is the potential for new guidance on what non-GAAP measures to use, where to use them and how to present them. Thus non-GAAP measures (the current use of which requires significant explanation and presentation merely to justify their use) will potentially be “in” again.
- (10) **Is the world really going to change?:** Some of these proposed changes would have a significant effect operationally on how things function in the “real world.” It will be interesting to watch how the SEC staff reacts to certain recommendations.

## *Appendix*

We have included the Advisory Committee's recommendations below, as provided in the four chapters of the Committee's report. The 25 recommendations are presented with some explanatory comments to describe their purpose and context.

### **Chapter 1**

Financial statements for virtually all public companies in the U.S. are generally prepared using US generally accepted accounting principles (GAAP). The application of GAAP can involve the use of estimates and judgments which may lead to inconsistencies among financial statements. The committee identified what it felt were the four most critical issues that contribute to potential inconsistencies and complexities: (1) the mixed attribute model that blends the use of fair value and historical cost, (2) the lack of a holistic approach to disclosures, (3) certain bright line thresholds, and (4) exceptions to general principles. These are discussed further below along with the related recommendations.

- (1) The mixed attribute model results in the use of three measurement methods in different situations: historical cost, lower of cost or market, or fair value. Additional complexity arises due to the current requirement to make some – or some portions of – related adjustments to earnings and others to equity. The Advisory Committee's recommendation to reduce complexities caused by this mixed attribute model are:

#### Recommendation 1.1

Reduce avoidable complexity caused by the mixed attribute model by addressing both the measurement framework and financial statement preparation.

- The SEC should recommend that the FASB be judicious in issuing new standards and interpretations that expand the use of fair value in areas where it is not already required until the FASB completes a measurement framework to systematically assign measurement attributes to different types of business activities and the SEC, the FASB, and other regulators and standards-setters develop and implement a plan to strengthen the infrastructure that supports fair value reporting.
  - The SEC should recommend that the FASB: (a) assign a single measurement attribute within each business activity to the maximum extent feasible, which is consistent across the financial statements, (b) aggregate business activities into operating, investing, and financing sections, and (c) add a new primary financial statement (the so-called "valuation roadmap" financial statement) to reconcile the statements of income and cash flows by major classes of measurement attributes to help investors analyze earnings.
- (2) Disclosures add additional perspective on financial statement information as well as highlight risks not included or evident in the statements that may impact future financial performance. To ensure disclosures are meaningful to investors, the Advisory Committee recommended:

### Recommendation 1.2

The SEC should recommend that the FASB develop a disclosure framework to:

- (a) Integrate existing disclosure requirements into a cohesive whole to ensure meaningful communication and logical presentation of disclosures, based on consistent objectives and principles. This framework would eliminate redundancies and provide a single source of disclosure guidance across all financial reporting standards. This framework could potentially end duplicative disclosures on a variety of topics from accounting policies, summary data and property holdings to litigation and financial commitments which are presently in both the “forepart” and the “F pages” of most SEC filings.
- (b) Require disclosure of the principal assumptions, estimates, and sensitivity analyses that may impact a company’s business, as well as a qualitative discussion of the key risks and uncertainties that could significantly change these amounts over time. This would encompass transactions recognized and measured in the financial statements, as well as events and uncertainties that are not recorded, such as certain litigation and regulatory developments.

### Recommendation 1.3

The SEC and FASB should also establish a process of coordination for the SEC to regularly update and, as appropriate, remove portions of its disclosure requirements as new FASB standards are issued.

- (3) Bright lines are defined thresholds that are meant to provide consistent results when used to apply U.S. GAAP. They are sometimes criticized as not allowing for adequate interpretation or consideration of relevant factors that could impact the accounting result. To ensure financial statements better reflect the substance of the underlying transaction, the Advisory Committee recommended:

### Recommendation 1.4

Recognition guidance in U.S. GAAP should be based on a recommendation that the recognition guidance in new projects undertaken jointly or separately by the FASB avoid the use of bright lines in favor of proportionate recognition (which means accounting for one’s rights and obligations as a party to a contract in contrast to the current all-or-nothing recognition approach under U.S. GAAP), which is consistent with certain current provisions found in, and allowed or required by, IFRS. Where proportionate recognition is not feasible or applicable, the FASB should provide qualitative factors in its recognition guidance. Finally, enhanced disclosure should be used as a supplement or alternative to the two aforementioned approaches. Any new projects should also include the elimination of existing bright lines in the recognition guidance of relevant areas to the extent feasible as a specific objective of those projects, in favor of the two aforementioned approaches.

### Recommendation 1.5

Constituents should be better trained to consider the economic substance and business purpose of transactions in determining the appropriate accounting, rather than relying on mechanical compliance with rules. As such, the SEC should undertake efforts, and also

recommend that the FASB, academics, and professional organizations, better educate students, investors, preparers, external auditors, and regulators in this respect.

(4) The Advisory Committee believes that exceptions to general principles should be eliminated so that similar activities are accounted for similarly. The Committee recommended:

#### Recommendation 1.6

U.S. GAAP should be presumptively based on business activities, rather than industries. The SEC should recommend that any new projects undertaken jointly or separately by the FASB be scoped on the basis of business activities, except in rare circumstances. Any new projects should include the elimination of existing industry-specific guidance – particularly that which conflicts with generalized U.S. GAAP – in relevant areas as a specific objective of those projects, except in rare circumstances.

Considering the pace of convergence efforts, the SEC should also recommend that, in conjunction with its current codification project, the FASB add a project to its agenda to eliminate existing industry-specific guidance which conflicts with generalized U.S. GAAP, except in rare circumstances.

#### Recommendation 1.7

U.S. GAAP should be based on a presumption that formally promulgated alternative accounting policies should not exist. Therefore, the SEC should recommend that any new projects undertaken jointly or separately by the FASB not provide additional options, except in rare circumstances. Any new projects should also include the elimination of existing alternative accounting policies in relevant areas as a specific objective of those projects, except in rare circumstances.

#### Recommendation 1.8

U.S. GAAP should be scoped with sufficient precision to minimize the use of scope exceptions. The SEC should recommend that any new projects undertaken jointly or separately by the FASB should be carefully scoped to minimize the use of exceptions. Any new projects should also seek to refine the scope of existing standards in relevant areas as a specific objective of those projects to minimize existing scope exceptions.

#### Recommendation 1.9

U.S. GAAP should be based on a presumption that similar activities should be accounted for in a similar manner. The SEC should recommend that any new projects undertaken jointly or separately by the FASB should not create additional competing models, except in rare circumstances. Any new projects should also include the elimination of competing models in relevant areas as a specific objective of those projects, except in rare circumstances.

## **Chapter 2**

The Advisory Committee believes a robust accounting standards-setting process is key to an efficient financial accounting and reporting process that is meaningful to investors. In the U.S., the evolution of U.S. GAAP has included many interpretations, exceptions and alternatives from a variety of sources which has resulted in increased complexity and therefore arguably either less meaningful or less comparable financial statements (or both).

To increase the consideration of the perspectives of investors in standard-setting, the Advisory Committee issued its so-called “open tent” recommendation:

#### Recommendation 2.1

Investor perspectives are critical to effective standards-setting, as investors are the primary consumers of financial reports. Only when investor perspectives are properly considered by all parties does financial reporting meet the needs of those it is primarily intended to serve. Therefore, investor perspectives should be given pre-eminence by all parties involved in standards-setting. Although it is more challenging to obtain investor perspectives than those of other constituents involved in the standards-setting process, additional investor representation would facilitate increased consideration of investor perspectives in the standards-setting process. Specifically, the SEC should recommend that the FAF and the FASB do the following:

- Add investors to the FAF to give more weight to the views of different types of investors, both large and small
- Give more representation on both the FASB and the FASB staff to experienced investors to improve consideration of the usefulness of financial reports
- Re-evaluate the manner, timing, and quality of investor input received throughout standards-setting to determine whether changes would be warranted to make investor involvement more efficient and effective.

To enhance governance and oversight of the standards-setting process, the Advisory Committee recommends:

#### Recommendation 2.2

The SEC should continue to recommend that the FAF enhance governance of the FASB, as follows:

- Recommend that the FAF amend the FASB’s mission statement, stated objectives, and precepts to emphasize that an additional goal should be to minimize avoidable complexity
- Recommend that the FAF develop performance metrics to ensure that key aspects of the standards-setting process are effective, efficient, and compliant with the goals in the FASB’s mission statement, objectives, and precepts.

To improve the standards-setting process the Advisory Committee recommends:

#### Recommendation 2.3

The SEC should recommend that the FAF, the FASB, and other participants in the financial reporting system continue to improve the effectiveness, efficiency, and timeliness of standards-setting, as follows:

- Create a formal Financial Reporting Forum (FRF) that includes key decision makers in the U.S. financial reporting system, including representatives from the SEC, the FASB, and the PCAOB, as well as the preparer, external auditor, and investor and other user communities, to make recommendations for responding to immediate needs and longer-

term priorities in the financial reporting system overall. This may require the FASB to re-evaluate the roles and composition of other advisory groups or agenda committees.

- Enhance the consistency and transparency of key aspects of the FASB's field work, including cost-benefit analyses, field visits and field tests.
- Formalize post-adoption reviews of each significant new standard to address interpretive questions and reduce the diversity of practice in applying the standard, if needed.
- Formalize periodic assessments of existing standards to keep the standards current.

To clarify the role of interpretive implementation guidance the Advisory Committee proposed the following two recommendations:

#### Recommendation 2.4

The SEC should coordinate with the FASB to clarify roles and responsibilities regarding the issuance of interpretive implementation guidance, as follows:

- To the extent practicable, going forward, there should be a single standards-setter for all authoritative accounting standards and interpretive implementation guidance that are applicable to a particular set of accounting standards, such as U.S. GAAP or IFRS. For U.S. GAAP, the FASB serves this function. To that end, the SEC should only issue broadly applicable interpretive implementation guidance in limited situations (see Recommendation 2.5).
- The FASB Codification, a draft of which was released for verification on January 16, 2008, should be completed in a timely manner. In order to fully realize the benefits of the FASB's codification efforts, the SEC should ensure that the literature it deems to be authoritative is integrated into the FASB Codification to the extent practicable, or separately codified, as necessary.
- All other sources of interpretive implementation guidance should be considered non-authoritative and should not be required to be given more credence than any other non-authoritative sources that are evaluated using reasonable judgments made in good faith that are supportable under U.S. GAAP.
- The proposed FRF should advise the FASB on re-prioritizing its agenda in a way that balances the need for international convergence (which is highly dependent on possible future actions of the SEC), improvements to the conceptual framework and maintenance of existing U.S. GAAP. If U.S. GAAP will continue to be in use for an extended period of time, such a re-prioritization of standards-setting should consider the possibility of a second phase of the codification project to systematically revisit U.S. GAAP.

#### Recommendation 2.5

As a general matter, the SEC staff should refrain from issuing broadly applicable interpretive implementation guidance that would change U.S. GAAP and instead should refer such matters to the FASB, such as through the proposed Financial Reporting Forum. The SEC staff should re-emphasize that its comment letter and "pre-clearance" processes are registrant-specific and that other registrants should respond to those comments by changing their accounting only after concluding it is appropriate to do so. Furthermore, the SEC staff is taking a number of steps to

improve the consistency of its interpretive implementation guidance associated with U.S. GAAP and the Commission should take appropriate steps to monitor the outcome of those actions.

If Recommendations 2.4 and 2.5 were adopted, it would bring an end to the ever evolving world of “speech GAAP” and “comment letter GAAP.” A fundamental question is whether the SEC staff would be willing to give up its “we’ll let you know” power as it would have a significant effect operationally on how things function in the “real world.” Therefore, it will be interesting to watch how the SEC staff reacts to these recommendations.

To improve the design of standards going forward, the Advisory Committee recommends:

#### Recommendation 2.6

The SEC should recommend that the FASB build upon recent improvements made to the design of accounting standards as part of its Understandability initiative – primarily by increasing the use of clearly-stated objectives, outcomes, and principles, and emphasizing the importance in financial reporting of the faithful representation of the economics of transactions and being responsive to investor and other user needs for clarity, transparency, and comparability.

### **Chapter 3**

Chapter 3 of the Advisory Committee’s report covers recommendations related to (1) financial restatements, including providing guidance on the materiality and correction of errors, and (2) the use of judgment in accounting, specifically whether it would be beneficial to provide guidance on the evaluation of judgments. These recommendations are intended to bring some sanity to the “restate (or not) process.” Each is discussed below.

#### (1) Financial restatements

Regarding the assessment of the materiality of financial statement errors and the correction of those errors, the Advisory Committee has four recommendations:

#### Recommendation 3.1

The FASB or the SEC, as appropriate, should supplement existing guidance to reinforce the following concepts:

- All of those who evaluate the materiality of an error (companies, external auditors, the SEC and the external auditors’ regulators – the PCAOB) should make the decision based upon the perspective of a reasonable investor
- Materiality should be judged based on how an error affects the total mix of information available to a reasonable investor.

Just as qualitative factors may lead to a conclusion that a small error is material, qualitative factors also may lead to a conclusion that a large error is not material.

The FASB or the SEC, as appropriate, should also conduct both education sessions internally and outreach efforts to financial statement preparers and external auditors to raise awareness of these issues and to promote more consistent application of the concept of materiality.

### Recommendation 3.2

The FASB or the SEC, as appropriate, should issue guidance on how to correct an error consistent with the principles outlined below:

- Companies should be required to correct all errors promptly and should not have the option to defer correction of errors until future financial statements. All material errors in previously issued financial statements should be disclosed when they are corrected.
- Prior period financial statements should only be restated for errors that are material to those prior periods.
- The determination of how to correct a material error should be based on the needs of investors making current investment decisions. For example, a material error that is not important to a current investment decision would not require restatement of the financial statements in which the error occurred, but would need to be promptly corrected and prominently disclosed in the current period financial statements.
- There may be no need for the filing of amendments to previously filed annual or interim reports to reflect restated financial statements, if the next annual or interim period report is being filed in the near future and that report will contain all of the relevant information.
- Restatements of interim periods do not necessarily need to result in a restatement of an annual period.
- Corrections of large errors in previously issued financial statements should always be disclosed in the filing, even if the error is determined not to be material.
- To limit the likelihood of “stealth restatements,” the SEC should revise the instructions to Form 8-K to state clearly that the form needs to be filed for all determinations of non-reliance on prior financial statements.

### Recommendation 3.3

The FASB or the SEC, as appropriate, should issue guidance on disclosure of financial information during the period in which a restatement is being prepared, about the need for a restatement and about the restatement itself to improve the adequacy of this disclosure based on the needs of investors.

### Recommendation 3.4

The FASB or the SEC, as appropriate, should develop and issue guidance on applying materiality to errors identified in prior interim periods and how to correct these errors. This guidance should reflect the following principles:

- Materiality in interim period financial statements must be assessed based on the perspective of the reasonable investor
- When there is a material error in an interim period, the guidance on how to correct that error should be consistent with the principles outlined in Recommendation 3.2.

## (2) Use of judgment

The use of judgment has received more focus in part due to the emphasis on principles-based standards, changes to external auditor regulation, and the increased use of fair value estimates. The goals of potential guidance related to judgments include: increasing investors' confidence in the use of judgments; reducing preparers concerns that judgments are not respected; coming to an agreement in principle on the criteria used to evaluate judgment; and decreasing concerns over the use of principles-based standards. To achieve these goals, the Advisory Committee recommends the following to create more transparency into the SEC's and PCAOB's thought process around evaluating judgments:

### Recommendation 3.5

The SEC should issue a statement of policy articulating how it evaluates the reasonableness of accounting judgments and include factors that it considers when making this evaluation. The PCAOB should also adopt a similar approach with respect to auditing judgments.

The statement of policy applicable to accounting-related judgments should address the choice and application of accounting principles, as well as estimates and evidence related to the application of an accounting principle. The Committee is of the view that a statement of policy that is consistent with the principles outlined in this recommendation to cover judgments made by external auditors based on the application of PCAOB auditing standards would be beneficial to external auditors. Therefore, the Committee recommends that the PCAOB develop and articulate guidance related to how the PCAOB, including its inspections and enforcement divisions, would evaluate the reasonableness of judgments made based on PCAOB auditing standards. The PCAOB's statement of policy should acknowledge that the PCAOB would look to the SEC's statement of policy to the extent the PCAOB would be evaluating the appropriateness of accounting judgments as part of an external auditor's compliance with PCAOB auditing standards.

The Committee asserted that it would be useful if the SEC also set forth in the statement of policy factors that it looks to when evaluating the reasonableness of preparers accounting judgments.

## **Chapter 4**

The recommendations in Chapter 4 result from the Advisory Committee's review of investor's information needs, how information is provided to investors, and ways to improve the delivery of financial information. The focus is on financial information provided by reporting companies in their periodic and current reports under the Securities Exchange Act of 1934 ("Exchange Act") and other ongoing disclosures provided by reporting companies to investors and the market.

At the present time, it is unclear whether the external auditor community will be expected to weigh in on these proposed reporting requirements with an opinion or other form of assurance. Underwriter behavior will likely influence developments in this area when comfort letter requests start to address filings which incorporate these new disclosures.

To help ensure that interactive data is a significant aspect of financial reporting in the future, the Advisory Committee recommends:

#### Recommendation 4.1

The SEC should, over the long-term, mandate the filing of interactive data-tagged financial statements after the satisfaction of certain preconditions relating to: (1) successful XBRL U.S. GAAP Taxonomy testing, (2) the capacity of reporting companies to file interactive data-tagged financial statements using the new XBRL U.S. GAAP Taxonomy on the SEC's EDGAR system, and (3) the ability of the EDGAR system to provide an accurately rendered version of all such tagged information. The SEC should phase-in interactive data-tagged financial statements as follows:

- The largest 500 domestic public reporting companies based on unaffiliated market capitalization (public float) should be required to furnish to the SEC, as is the case in the voluntary program today, a document prepared separately from the reporting companies' financial statements that are filed as part of their periodic Exchange Act reports. This document would contain the following:
  - Interactive data-tagged face of the financial statements
  - Block-tagged footnotes to the financial statements.
- Domestic large accelerated filers (as defined in SEC rules, which would include the initial 500 domestic public reporting companies) should be added to the category of companies, beginning one year after the start of the first phase, required to furnish interactive data-tagged financial statements to the SEC.

Once the preconditions noted above have been satisfied and the second phase-in period has been implemented, the SEC should evaluate whether and when to move from furnishing a document to the SEC to the official filing of interactive data-tagged financial statements with the SEC for the domestic large accelerated filers, as well as the inclusion of all other reporting companies, as part of a company's Exchange Act periodic reports.

To improve the use of corporate websites to provide corporate information and developments the Advisory Committee recommends:

#### Recommendation 4.2

The SEC should issue a new comprehensive interpretive release regarding the use of corporate websites for disclosures of corporate information, which addresses issues such as liability for information presented in a summary format, treatment of hyperlinked information from within or outside a company's website, treatment of non-GAAP disclosures and GAAP reconciliations, and clarification of the public availability of information disclosed on a reporting company's website. (Note that the SEC has addressed this recommendation. See Protiviti's SEC Flash Report dated August 1, 2008.)

Industry participants, including investors, should coordinate among themselves to develop uniform best practices on uses of corporate websites for delivering corporate information to investors and the market.

To improve the effectiveness of key performance indicators (KPIs) reporting and increase user understanding, the Advisory Committee recommends:

Recommendation 4.3

The SEC should encourage private sector initiatives targeted at best practice development of company use of KPIs in their business reports. The SEC should encourage private sector dialogue, involving preparers, investors (including analysts), and other interested industry participants, such as consortia that have long supported KPI-like concepts, to generate understandable, consistent, relevant and comparable KPIs on relevant activity and, as appropriate, industry-specific, bases. The SEC also should encourage companies to provide, explain and consistently disclose period-to-period company-specific KPIs. The SEC should consider reiterating and expanding its interpretive guidance regarding disclosures of KPIs in MD&A and other company disclosures.

To improve quarterly press release disclosures and timing, the Advisory Committee recommends:

Recommendation 4.4

Industry groups, including the National Investor Relations Institute, FEI, and the CFA Institute should update their best practices for earnings releases. Such updated best practices guidance should cover, among other matters, the type of information that should be provided in earnings releases and the need for investors to receive information that is consistent from quarter to quarter, with an explanation of any changes in disclosures from quarter to quarter. Further, the best practices guidance should consider recommending that companies include in their earnings releases the income statement, balance sheet and cash flow tables, locate GAAP reconciliations in close proximity to any non- GAAP measures presented, and provide more industry and company specific key performance indicators.

The SEC should consider restating its view that disclosures in connection with earnings calls posted on company websites should be maintained and available on such sites for at least 12 months.

To encourage the use of executive summaries and increase the usability of periodic reports by all investors, the Advisory Committee recommends:

Recommendation 4.5

The SEC should mandate the inclusion of an executive summary in the forepart of a reporting company's filed annual and quarterly reports [or, alternatively, annual reports initially with a phase-in for quarterly reports] that will provide a roadmap to the fuller discussion in the reports. The executive summary should provide summary information, in plain English, in a narrative and perhaps tabular format of the most important information about a reporting company's business, financial condition, and operations. As with the MD&A, the executive summary should be required to use a layered approach that would present information in a manner that emphasizes the most important information about the reporting company and include cross-references to the location of the fuller discussion in the periodic report. To the extent a similar summary is included elsewhere in the report, the disclosure could cross-reference such summary. The requirement for the executive summary, with a recommended length of up to two pages, should build on, but not replicate, the company's MD&A

overview and essentially be principles-based, other than a limited number of required disclosure items such as:

- A summary of key aspects of company performance;
- A digest of the company's GAAP, non-GAAP and non-financial KPIs (to the extent disclosed in the company's Form 10-Q or 10-K [or, alternatively, to the extent disclosed in the company's Form 10-K]);
- A summary of business outlook; and
- Page number references to more detailed information contained in the document (which, if the report is provided electronically, could be hyperlinks).