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2021 FINANCIAL RESTATEMENTS

A TWENTY-ONE-YEAR REVIEW

May 2022

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EXECUTIVE SUMMARY

Restatements climbed to highest level since 2006.

The number of restatements filed increased significantly to 1,470, due to SPAC restatements. Excluding SPAC restatements, there was a 10% year-over-year *decrease*.

Debt and equity became top cited accounting issue.

Revenue recognition had been the top issue in each of the past 3 years. But debt and equity accounting was 2021's top issue, both including and excluding SPAC restatements.



INTRODUCTION

Financial restatements are a significant measure of financial reporting quality. A financial restatement occurs when a company discovers an error or misstatement in previously issued financial statements, and they correct that error by adjusting previous periods.

Companies have three methods for correcting errors and misstatements in financial statements:

- Reissuance restatements,
- Revision restatements, or
- Out-of-period adjustments.

Reissuance restatements are material errors and misstatements announced in a form 8-K item 4.02. The announcement is followed by the reissuance of previous financial statements with corrected financial information.



Revision restatements are immaterial errors and misstatements that are corrected by revising the previous periods in the current financial report. These restatements are disclosed in the footnotes of the current financial statements rather than in a separate notification.

Out-of-period adjustments are immaterial errors and misstatements that are corrected in the current period of the current financial report. These are not restatements because previous financial statements are not affected. This report does not include a review of out-of-period adjustments.

Once an error or misstatement has been identified, the company must evaluate its materiality to determine the restatement method.

If a company decides that the correction of an error or misstatement would affect a reasonable investor's assessment of a company's results, they should correct the error with a reissuance restatement.

However, if the correction of the error or misstatement would not influence a reasonable investor, the company should correct the error with a revision restatement or an out-of-period adjustment, depending on whether correcting the error in the current period would have a material impact on the financial statements.

The distinction in the restatement method is important because the goal of financial reporting is to provide accurate, timely, and decision-useful information. The occurrence of a material error impairs the usefulness of previously reported financial information.

Determining Materiality

Guidance on determining the materiality of an error or misstatement is outlined and provided by:

- Securities and Exchange Commission's (SEC) Staff Accounting Bulletin (SAB) Topic 1.M, also known as SAB 99.1
- SAB Topic 1.N, also known as SAB 108, provides further clarification from SEC staff on how to apply quantitative analyses of materiality.²
- The application of accounting standards for correcting errors and misstatements is codified under the Financial Accounting Standards Board's (FASB) Accounting Standard Codification (ASC) 250-10-45.

2021 RETROSPECTIVE

SPAC-Centered Restatements and Implications for Trend Analysis

On April 12, 2021, the SEC's Acting Director of the Division of Corporation Finance John Coates and Acting Chief Accountant Paul Munter issued a joint statement urging companies with warrants issued by Special Purpose Acquisition Companies (SPACs) to reconsider the accounting treatment of those warrants.³ In November, hundreds of SPACs reclassified redeemable shares from permanent equity to temporary equity.

The SEC's guidance on accounting for redeemable shares and warrant liabilities resulted in significant increases observed in both the number of restatements filed and the number of companies that disclosed a restatement during 2021. Additionally, the composition of restating companies was altered from previous years, as these two accounting issues had a broad impact on a narrow population: SPACs and companies acquired by SPACs.

Discussed throughout this report, these restatements have a pervasive impact on historical trend analysis, disrupting over a decade of observed trending.

"SPAC-CENTERED RESTATEMENTS"

To account for the anomaly in observed annual trending caused by restatements related to redeemable shares and warrant liabilities, this report classifies these restatements as "SPAC-centered restatements." In denoted analyses, these restatements are excluded from general restatements to highlight anticipated vs. realized trends.

2021 Restatement Composition





Redeemable Shares

Only SPACs were impacted by accounting issues related to redeemable shares. Most SPACs recorded shares that included a redeemable feature as permanent equity. The SEC objected to the classification of redeemable shares as permanent equity and requested the shares be recorded as temporary equity.

More than **500 companies** reclassified redeemable shares from permanent equity to temporary equity.

Warrant Liabilities

SPACs *and* companies taken public via SPAC were impacted by issues related to accounting for warrants. Most SPACs recorded warrants as equity at historical cost. In a statement, the SEC asked companies to consider whether the shares were indexed or whether the shares included a tender offer provision. Generally, warrants that are not indexed to a company's own stock or that include a tender offer provision should be recorded as a liability with fair value adjustments recorded on a quarterly basis through the income statement.

More than **600 warrant restatements** were disclosed following the SEC's statement.

OVERVIEW



The total number of restatements and the number of unique companies that disclosed a restatement rose to their highest levels since 2006. The rise is in contrast to the decline seen during the previous decade.

In 2021, total restatements increased by 289%, and unique companies that disclosed a restatement rose by 194%.

EXCLUDING SPAC-CENTERED RESTATEMENTS IN 2021:

The total number of restatements **declines by 10%.**

The number of unique companies that disclosed a restatement **declines by 15%.**



Percentage of Unique Company Restatements



The decline in restatements during the previous decade has been due, in part, to both improved reporting and a decline in SEC registrants.

Improved reporting resulted in the percentage of companies that disclosed a restatement during 2020 reaching a low of just 4.8%. And the number of SEC registrants that filed an annual or quarterly financial report with the SEC declined from more than 10,000 unique companies during 2010 to just 7,300 unique companies during 2020.

The popularity of SPACs increased the number of SEC registrants during 2021, climbing to over 8,000.

Due to the influx of new SPAC SEC registrants, 2021's SPAC-centered restatements increased the percentage of unique companies that disclosed a restatement to 12.7%, slightly trailing the 13.6% high point observed during 2006.

More SPACs, More Companies Restating

2021's SPAC-centered restatements increased the percentage of unique companies that disclosed a restatement during the year.



MATERIALITY

Disclosure of Material Misstatements

Misstatements that are material must be disclosed in a Form 8-K, Item 4.02, referred to as reissuance, non-reliance, or "Big-R" restatements. The use of Form 8-K **excludes Foreign Private Issuers** (FPIs) - companies that use Forms 20-F or 40-F to issue annual reports - from the 8-K, Item 4.02 disclosure requirement.



Domestic issuers represent most SEC registrants. These issuers disclose the majority of restatements.

However, in recent years FPIs began disclosing a larger proportion of restatements.

This observed trend reversed during 2021 because SPACs are overwhelmingly Domestic filers.

More Domestic SPACs, Smaller Proportion of FPI Restatements

Previous trending showed a greater proportion of total restatements disclosed by FPIs in recent years. But this trending reversed in 2021, in part, because the proportion of restatements for Domestic filers was bolstered by SPACs.

Restatements by Registrant Type



Reissuance Restatements - Domestic Filers



The requirement for Domestic filers to disclose material restatements in form 8-K, Item 4.02, began in August 2004. Since 2005 - the first full year of the requirement - reissuance restatements have declined as a proportion of total restatements. This trend reversed in 2021 due to warrant and redeemable share SPAC-centered restatements.

EXCLUDING SPAC-CENTERED RESTATEMENTS IN 2021:

The proportion of reissuance restatements for domestic filers aligns with previous years.





Revision Restatements - Domestic Filers

IMPACTS

Average Restatement Income Impact



Largest Negative Income Impact

Disclosur Year	e Company Name	Market	Income Impac in millions (USD)
2003	ENCOMPASS HEALTH CORP (formerly HealthSouth Corp)	NYSE	-3,998
2004	FEDERAL NAT'L MORT. ASSOC. (Fannie Mae)	NYSE	-6,335
2005	AMERICAN INTERNATIONAL GROUP INC	NYSE	-5,193
2006	NAVISTAR INTERNATIONAL CORP	NYSE	-2,377
2007	GENERAL ELECTRIC CO	NYSE	-341
2008	TMST INC	NYSE	-671
2009	UBS AG	NYSE	-375
2010	TIM S P A (formerly Telecom Italia S P A)	NYSE	-717
2011	CHINA UNICOM (HONG KONG) LTD	NYSE	-1,557
2012	LEAR CORP	NYSE	-1,204
2013	QUICKSILVER RESOURCES INC	NYSE	-420
2014	COMPUTER SCIENCES CORP	NYSE	-286
2015	ALPHABET INC	Nasdaq	-711
2016	ING GROEP NV	NYSE	-1,085
2017	PERRIGO CO PLC	NYSE	-1,177
2018	OI S.A. (formerly Brasil Telecom SA)	NYSE	-1,993
2019	BAXTER INTERNATIONAL INC	NYSE	-276
2020	WPP PLC	NYSE	-980
2021	PERSHING SQUARE TONTINE HOLDINGS LTD	NYSE	-953

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Impact on Net Income





EXCLUDING SPAC-CENTERED RESTATEMENTS IN 2021:

32% of restatements had a **negative impact** on net income.

What is the difference between Foreign Private Issuer and Domestic Filer?

The SEC has two tests to determine if a foreign issuer meets the definition of a Foreign Private Issuer (FPI).*

Test 1:

If 50% of outstanding shares are owned by non-US residents.

Test 2:

If all of the following apply:

- 1. The majority of executive officers or directors are non-US citizens or residents.
- 2. 50% or more of the issuer's assets are located outside of the US; or
- 3. The business of the issuer is administered principally outside of the US.

An issuer that passes Test 1 is eligible to be an FPI. If an issuer fails Test 1, that issuer must pass all Test 2 criteria to be eligible to be an FPI.

Any issuer that is headquartered outside of the US and fails both Test 1 and any part of Test 2 is considered a Domestic filer.

*FPI definition based on Rule 405 of the Securities Act. https://www.ecfr.gov/current/title-17/chapter-II/part-230/subject-group-ECFR3ba3c08ffc29ca2/section-230.405



SEVERITY MEASURES

Average Issues per Restatement

The number of issues disclosed per restatement can help financial statement users understand the severity of the error or misstatements. More issues relate to poorer financial control systems.

> **Average Number of Issues** 2002 2.16 2003 2.18 2004 2.18 2005 2.46 2006 2.01 2007 1.92 2008 1.67 2009 1.51 2010 1.54 2011 1.55 2012 1.52 2013 1.67 2014 1.74 2015 1.67 2016 1.61 2017 1.60 2018 1.64 2019 1.53 2020 1.52 2021 1.85

EXCLUDING SPAC-CENTERED RESTATEMENTS IN 2021: The average issues per restatement is **1.4**

Percentage of Annual Restatements

The restatement of an annual report can reflect the severity of a restatement because annual reports must be audited by an independent accounting firm. An error or misstatement in an annual report is not only missed by management but also by the firm conducting the audit.

Annual	Quarterly	
68%	32%	2002
67%	33%	2003
71%	29%	2004
80%	20%	2005
71%	29%	2006
67%	33%	2007
63%	37%	2008
63%	37%	2009
64%	36%	2010
66%	34%	2011
66%	34%	2012
68%	32%	2013
65%	35%	2014
64%	36%	2015
67%	33%	2016
68%	32%	2017
59%	41%	2018
60%	40%	2019
58%	42%	2020
33%	67%	2021

EXCLUDING SPAC-CENTERED RESTATEMENTS IN 2021:

Annual restatements are 61%

		480,091.00	512,603.00	550,009.00	3,955, 00	2,580,255.00	1,835,094.00	\$8,520.00	22,84
*	0 3,156.00	37,872.00	37,872.00	37,872.00	3 72.00	37,872.00	37,872.00	3,184.00	1,00
	3,907.00	46,884.00	46,884.00	46,884.00	384.00	46,884.00	46,884.00	1 1,448.00	1,3
	4,250.00	51,000.00	51,000.00	51,000.00	,000.00	51,000.00	51,000.00	1, ,000.00	1,42
	1,327.00	15,924.00	15,924.00	15,924.00	5,924.00	15,924.00	15,924.00	3 465.00	48
	1,142.00	13,704.00	13,704.00	13,704.00	3,704.00	13,704.00	13,704.00	662.00	15
	4,890.00	58,680.00	58,680.00	58,680.00	\$,680.00	58,680.00	58,680.00	4 100.00	79
	1,264.00	15,168.00	15,168.00	15,168.00	,168.00	15,168.00	15,168.00	096.00	23
100	1,366.00	16,392.00	16,392.00	16,392.00	\$92.00	16,392.00	16,392.00	1,744.00	21
	231.00	14,772.00	14,772.00	14,772.00	14 .00	14,772.00	14,772.00	10,334.00	22
	19.00	31,428.00	31,428.00	31,428.00	31,4 00	534,457.00	45,573.00	442,344.00	4,14
	0.00	55,320.00	55,320.00	9,220.00	234,423	234,233.00	45,344.0	24,423.00	65
910	.00	18,174.00	3,654.00	23,312.00	3,423.00	23,423.00	34,52	246,723.00	353
000		2,276.00	25,412.00	54,322.00	2,342.00	152.00	1.00	564,523.00	1,339
		15,726.00	15,256.00	33,245.00	3,423.00	34,422.00	42,234.00	34,233.00	178
		16,164.00	16,164.00	16,164.00	16,164.00	10,776.00	234,423.00	4,234,467.00	4,544
		30,404.00	30,707.00	30,707.00	010 10100				

Length of Restatement Period

Average Number of Days

A lengthy restatement period, measured as the number of days encompassed by the restatement, suggests that financial reporting systems have operated ineffectively for a longer amount of time, resulting in investors and other stakeholders consuming more inaccurate financial information.



Length of Disclosure Window

Average Number of Days

A long period of time between when a company announces the need to restate and when a company files the restatement can indicate a more complex error or misstatement in financials. Time is required to investigate the error, and, if necessary, produce new financials and obtain an audit of the corrected financials.



Note: This analysis only includes reissuance restatements because revision restatements are not announced prior to the financial statements being issued. The analysis only goes back to 2005 because this was the first full year the itemized Form 8-K included item 4.02 for reissuance restatements.



SIZE AND LOCATION

Restatements by Location



What Defines a Foreign Company?

Unlike the determination of a Foreign Private Issuer, the determination of a foreign company is based on where a company's headquarters is located. Companies with headquarters outside of the US are considered foreign companies.

Percentage of Restatements by Location



Restatements by Company Size - US



Restatements by Company Size - Foreign



2021 Restatements by Size and Location

United States	
Large Accelerated Filers	10.2%
Accelerated Filers	4.5%
Non-Accelerated Filers	73.1%
Foreign	
Large Accelerated Filers	1.4%
Accelerated Filers	0.4%
Non-Accelerated Filers	10.5%



ACCOUNTING ISSUES

Top 10 Most Common Issues Trends

Excluding SPAC-Centered Restatements (Redeemable Shares / Warrants)



Top 10 Accounting Issues of 2021

			Excluding SPAC-Ce (Redeemable S	ntered Restatements Shares / Warrants)
Restatement Issue	Citations	Frequency	Citations	Frequency
1. Debt and equity securities	1,182	80.4%	65	19.1%
2. Revenue recognition	41	2.8%	41	12.0%
3. Liabilities and accruals	41	2.8%	40	11.7%
4. Expenses	39	2.7%	37	10.9%
5.Taxes	30	2.0%	30	8.8%
6.Cash flows	25	1.7%	25	7.3%
7.Share-based compensation	25	1.7%	24	7.0%
8. Acquisitions and divestitures	25	1.7%	24	7.0%
9.Inventories	23	1.6%	23	6.7%
10.Asset valuations	23	1.6%	22	6.5%

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Restatement Accounting Issue Analysis: Top 5 Issues of 2021 Excluding SPAC-Centered Restatements (Redeemable Shares / Warrants)



DATABASE OVERVIEW

The Audit Analytics Financial Restatements database includes data from more than 18,000 financial restatements and/or non-reliance filings disclosed by over 10,000 SEC public registrants since January 1, 2001.

In addition to the areas identified in the charts contained in this report, the database employs a taxonomy (issue classifications) of more than 40 different accounting error categories (e.g., Cash Flow Statement, Tax, Revenue Recognition, Intangible Assets, etc.). Search results from this level of granularity can be filtered by other demographic data such as industry, financial size, filer status designation, location, audit firm, and any number of peer groups.

The relational nature of the database allows researchers to introduce and compare financial restatement search results into other data sets, such as accelerated filer status, legal exposures, director and officer changes, auditor changes, audit fees, internal control reports, and other data populations. This content extension further allows an analyst to identify anomalies and market patterns that would not be readily apparent without performing this layered approach.





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ABOUT US

Whether for market intelligence, risk management, compliance, or research and public policy, Audit Analytics provides the highly structured data you need to make informed decisions.

Our expert team meticulously collects, organizes, and analyzes data – making it easy for our customers to find what they need to know. We are trusted to simplify the complex; to illuminate trends; and to reveal actionable insights.

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