Audit Analytics®

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SOX 404 DISCLOSURES

A SIXTEEN YEAR REVIEW

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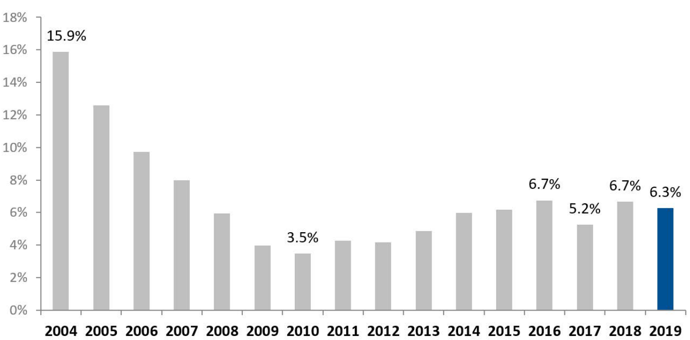
SOX 404 Disclosures: A Sixteen Year Review

Summary

In response to the Enron and Worldcom collapses, Congress passed the Sarbanes-Oxley Act of 2002 (SOX) to better protect investors. Section 404 of SOX (SOX 404) requires companies to review their internal controls over financial reporting (ICFR) and declare whether their ICFR are "effective" or "ineffective." In other words, they must determine if their ICFR are adequate enough to produce financial statements that are complete and accurate. SOX 404 has two requirements: a management assessment and an auditor attestation. Large companies (accelerated filers) must have their independent auditor attest to the management's assessment of ICFR. Smaller companies (non-accelerated filers), however, are not required to include an auditor attestation (a management-only assessment).

SOX 404 first applied to United States accelerated filers in their annual reports for fiscal years ending on or after November 15, 2004. By mid July 2007, SOX 404 also applied to all foreign accelerated filers. Non-accelerated filers began filing management-only assessments in annual reports for the fiscal years ending on or after December 15, 2007. The Dodd-Frank Act exempted non-accelerated filers from the auditor attestation requirement of SOX 404(b).

Adverse Auditor Attestations

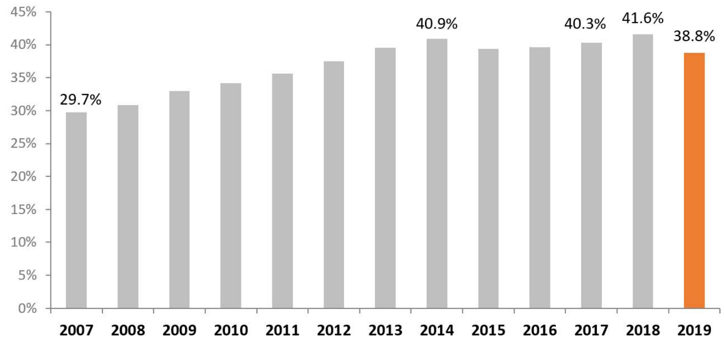


The percentage of Adverse Auditor Attestations experienced a local maximum in fiscal year 2016.

As shown in the graph above, 15.9% of accelerated filers that filed their first auditor attestation for fiscal year 2004 disclosed ineffective ICFR. After six years of consecutive improvements, this figure dropped to 3.5% for fiscal year 2010. During 2010 and 2011, however, PCAOB inspections of audits began to determine if the audit process obtained adequate evidence to substantiate the auditor's attestation of the management's assessment regarding the effectiveness of ICFR. This focus on the part of the PCAOB appears to have had an impact.

As the prior graph shows, the percentage of auditor attestations disclosing ineffective ICFR increased after the low in 2010 and reached a local maximum of 6.7% for fiscal year 2016. Fiscal year 2017 dropped to 5.2%, but the percentage bounced back up to 6.7% for 2018 then dropped to 6.3% for 2019.

Adverse Management-Only Assessments



After seven years of increases, Adverse Management-Only Assessments dropped in 2015 and has remained steady since.

A focus on management-only assessments reveals a different trend. As shown in the graph above, the percentage of small companies that disclosed ineffective ICFR rose steadily for seven consecutive years from 2008 to 2014 to a peak of 40.9%. Thereafter, the rate dropped to 39.4% and remained between 39% to 42% since. Adverse disclosure percentages have been above 39% since 2013. This value is a much higher ineffective rate than disclosed by accelerated filers. A review of the issues resulting in adverse disclosures found that personnel issues, such as inadequate training and the ability to avoid segregation of duty problems, were prominent reasons of concern within smaller companies.

Introduction

Both the Enron and Worldcom collapse culminated from a practice of disguising the true operating performance of the companies. In response to these meltdowns, Congress passed the Sarbanes-Oxley Act of 2002 (SOX). In its title, the declared purpose of SOX is to "protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes." One section of SOX, Section 404 (SOX 404), furthers this goal by instructing the Securities and Exchange Commission (SEC) to prescribe rules imposing a duty on officers and management to implement, review, and certify the effectiveness of a company's internal controls for financial reporting (ICFR).[1] In addition, the registered public accountant is to attest to and report on the management's assessment. In short, SOX 404(a) requires management to assess a company's ICFR while SOX 404(b) requires a registered public accountant to attest to the management's report.

SOX 404 Requirements History: The Staggered and Two-Tiered Implementation of SOX 404

SOX 404 Compliance Dates: Fiscal Year End Date of Annual Reports

SOX 404 Provision	Accelerated Filers			Non-Accelerated Filers
	United States	Foreign		
		Large Accelerated	Accelerated	
SOX 404(a)	Nov. 15, 2004 (both required)	July 15, 2006 (both required)	July 15, 2006	Dec. 15, 2007
SOX 404(b)			July 15, 2007	N/A

SOX 404 began to apply to different categories of companies at different times. Moreover, as summarized in the table on the right, the two subsections of SOX 404 did not necessarily come into effect at the same time. United States accelerated filers[2] were first required to provide SOX 404 certifications in annual reports for fiscal years ending on or after November 15, 2004. At that time both provisions were required: the management assessment (404(a)) and the auditor attestation (404(b)). During SOX 404's third year of application, its provisions began to apply a new category of public registrant: accelerated foreign filers. For year three, a large accelerated foreign filer was required to adhere to both provisions in its annual report for the fiscal year ending on or after July 15, 2006. However, an accelerated foreign filer that was not a large accelerated foreign filer was given a gradual two-tier requirement. That category of foreign filers was only required to provide a management assessment for July 15, 2006, and did not need to give an auditor attestation until the following year. In similar fashion, the SEC initially intended to apply a two-step approach to non-accelerated filers. Non-accelerated filers were required to provide a management assessment (but not an auditor attestation) in their annual reports for the fiscal years ending on or after December 15, 2007. Before subsection 404(b) became effective, however, the Dodd-Frank Act exempted the non-accelerated filers from the auditor attestation requirement.[3] Therefore, except for asset-backed securities and registered investment companies,[4] all SEC registrants are required to provide at least a management report and accompanying certifications[5] in their annual reports unless, pursuant to the Jumpstart Our Business Startups Act (the JOBS Act), the company falls within the five-year exemption provided to "emerging growth companies."[6]

Standards and PCAOB Oversight of Independent Auditors

To provide guidance for an independent auditor's review of a company's ICFR, the Public Company Accounting Oversight Board (PCAOB) issued Auditing Standard No. 5, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements (AS 5). This new standard applied to audits for fiscal year ends on or after November 15, 2007. During 2008 and 2009, PCAOB inspections of audits evaluated, among other things, the auditor's implementation of the new standards. The following year, the PCAOB shifted the review to determine if the audit process obtained adequate evidence to substantiate the auditor's attestation of the management's assessment regarding the effectiveness of ICFR.[7] After discovering a number of deficiencies during the 2010 and 2011 inspections, the PCAOB published a report in December 2012 titled "Observations from 2010 Inspections of Domestic Annually Inspected Firms Regarding Deficiencies in Audits of Internal Control over Financial Reporting." In October 2013, the PCAOB published Staff Audit Practice Alert No. 11, "Considerations for Audits of Internal Control Over Financial Reporting", to highlight the deficiencies observed and the responsibilities dictated by AS 5.

1 *In general, Section 404 requires that each annual report contain an "internal control report" that (1) acknowledges the management's responsibility to maintain adequate internal controls, (2) identifies the "framework" used to evaluate the effectiveness of the internal controls over financial reporting, and (3) provides an assessment of the effectiveness of these internal controls as of the end of the fiscal year.*

2 *An accelerated filer is a company whose public Float (as opposed to Market Capitalization) exceeds $75 million as of the last day of their second quarter. Once a registrant becomes an accelerated filer, it will not lose this status unless its float drops below $50 million. A large accelerated filer is a company whose public Float exceeds $700 million. See Rule 12b-2 of the Securities Exchange Act of 1934.*

3 *See Section 989G of the Dodd-Frank Wall Street Reform and Consumer Protection Act.*

4 *Registered investment companies are expressly exempt from Section 404 by Section 405 of SOX.*

5 *The SEC provides a form entitled "CERTIFICATIONS" to be attached to the annual report that contains the necessary language for a 404 certification. A separate copy of this form must be signed by both the CEO and CFO without any change in the language and attached as Exhibit 31.*

6 *The emerging growth company exemption replaced a one-year exemption for "newly public companies."*

7 *See transcript of Jeanette M. Franzel's speech, Effective Audits of Internal Control in the Current "Perfect Storm," given on March 26, 2014: www.pcaobus.org/News/Speech/Pages/03262014_IIA.aspx.*

Further guidance was provided by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in May 2013. In 2013, COSO published the *Internal Control — Integrated Framework* which, as stated by COSO, "is expected to help organizations design and implement internal control in light of many changes in business and operating environments since the issuance of the original Framework, broaden the application of internal control in addressing operations and reporting objectives, and clarify the requirements for determining what constitutes effective internal control."[8]

The issuance of this new standard, coupled with the PCAOB's emphasis on the auditors' responsibilities as they relate to their audit of ICFR, constitutes what PCAOB board member Jeanette Franzel calls the "perfect storm" in the efforts to improve ICFR.[9] The SEC, which has regulatory authority over public companies (unlike the PCAOB) also maintains a watchful eye over the status of ICFR. "It is hard to think of an area more important than ICFR to our shared mission of providing high-quality financial information that investors can rely on," stated SEC Chair, Mary Jo White.[10]

Similarly, in 2016, the Chief Accountant of the SEC publicly stated that ICFR are a focus and both the SEC and PCAOB "encourage regular discussions between management, auditors, and audit committees on existing and emerging issues in assessments of ICFR."[11]

SEC Enforcement of SOX 404

The SEC has demonstrated that it will not tolerate companies that are unable or unwilling to correct ineffective internal controls. On January 29, 2019, the SEC issued a press release announcing an investigation conducted by the Division of Enforcement's Financial Reporting and Audit Group (FRAud Group).[12] This investigation resulted in fines imposed on four companies with longstanding ICFR failures. The duration of the ongoing failures lasted between seven to ten consecutive years and resulted in civil penalties between $35,000 and $200,000.

Executive Summary - SOX 404 Disclosures Regarding Internal Controls over Financial Reporting

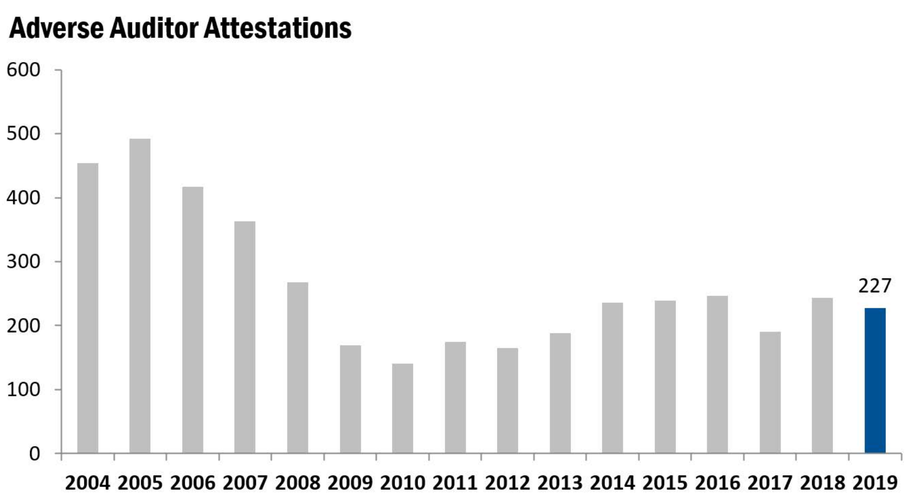
Auditor Attestations

As explained above, accelerated filers are required pursuant to SOX 404(b) to provide an auditor attestation of management's assessment of ICFR. Therefore, a review of auditor attestations focuses on disclosures provided by larger companies.

1. Total Number of Auditor Attestations Disclosing Ineffective ICFR.

Audit Analytics reviewed the population of SOX 404 auditor attestations and identified those that disclosed ineffective ICFR. Since 2004, the largest number of adverse attestations occurred during fiscal year 2005 with a total of 492 (*See Figure 1 and page 7*). Following 2005, the number of adverse attestations decreased for five consecutive years to a low of 141. Thereafter, the totals reflected a six-year upward trend, ostensibly due in part to the activities of the PCAOB and other oversight discussed above. This upward trend peaked in 2016 with a total of 247 adverse attestations, followed by a dramatic drop to 190 (an amount in line with the three-year period from 2011 to 2013). In 2018, however, the total rebounded to a value of 243, followed by a decline to 227 in 2019. As shown in Figure 1, five of the last six years have experienced totals over 200.

FIGURE 1



8 *See COSO website: http://www.coso.org/ic.htm.*

9 *See footnote 8 and, also, the transcript of Jeanette M. Franzel's speech, Current Issues, Trends, and Open Questions In Audits of Internal Control over Financial Reporting given on August 8, 2015: www.pcaobus.org//News/Speech/Pages/08102015_Franzel.aspx.*

10 *https://www.sec.gov/news/speech/keynote-2015-aicpa-white.html*

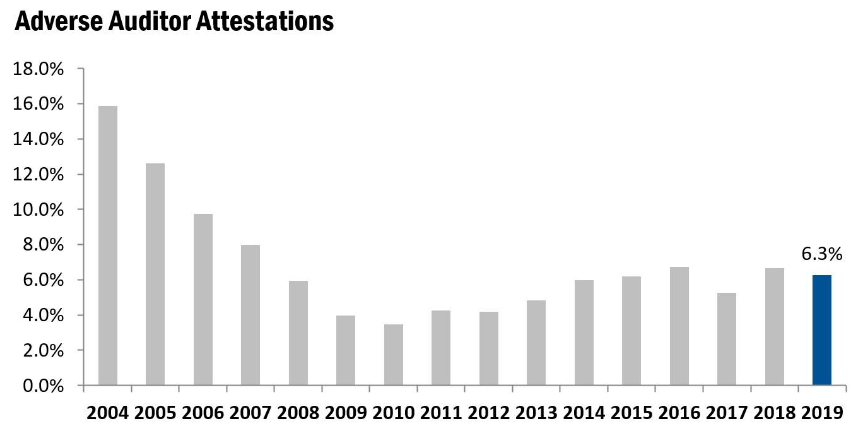
11 *See transcript of James V. Schnurr's speech, Remarks before the 12th Annual Life Sciences Accounting and Reporting Congress, given on March 22, 2016: www.sec.gov/news/speech/schnurr-remarks-12th-life-sciences-accounting-congress.html.*

12 *https://www.sec.gov/news/press-release/2019-6*

2. Total Percentage of Auditor Attestations Disclosing Ineffective ICFR.

Figure 2 shows the percentage of SOX 404 auditor attestations that disclosed ineffective ICFR. With the exception of 2004 and 2005, Figure 2 appears very similar to Figure 1 showing the total number of adverse attestations. In Figure 2, the highest percentage of adverse attestations was disclosed for fiscal year 2004. As noted above, 2004 included only those companies with fiscal years ending on or after November 15th. Therefore, even though 2004 had fewer adverse attestations than 2005, the fiscal year also had fewer total attestations: 2,859 in 2004 compared to 3,905 in 2005. (*See Figure 2 and page 7.*) After a high of 15.9% in 2004, six years of consecutive improvement occurred to reach a low of 3.5% in 2010. An upward trend followed with a local maximum of 6.7% in 2016, followed by a drop to 5.2% in fiscal year 2017, and an uptick back to 6.7% in 2018. The percentage dropped to 6.3% in 2019, but is similar to the trend in recent years: five of the last six years experienced a percentage of 6% or higher.

FIGURE 2



3. The Readiness of Companies Filing First Auditor Attestations.

As a company grows and begins to approach the accelerated filer threshold of $75 million in public float, it will trigger the auditor attestation provision in SOX 404(b) and bring higher scrutiny from their public auditors regarding the company's ICFR. Table 1 indicates the percentage of companies that approach this threshold inadequately prepared for the transition.

In addition, Table 1 quantifies how many auditor attestations were filed by companies that had not filed an attestation in the past (the first auditor attestation) during each year. The adjacent column indicates how many first-time attestations disclosed ineffective ICFR. As shown in the rightmost column, the percentage of adverse attestations from companies newly exposed to the requirements of SOX 404(b) varied from 5.88% to 22.27%. The value of 5.88% for 2012, however, appears to be an anomaly. In almost every other year, at least 10% of the companies filing their first auditor attestation disclosed a need to improve their ICFR. Fiscal year 2019 is the first year where the percentage exceeded 20%, with a value of 22.27% - substantially higher than the previous historic highs of around 17%.

TABLE 1

Negative Disclosure in First Attestation

Fiscal Year	Total # of First Auditor Attestation	Negative Attestation in First Attestation	% of Negative First Auditor Attestations
2004	2,859	454	15.88%
2005	1,279	221	17.28%
2006	686	73	10.64%
2007	678	88	12.98%
2008	434	62	14.29%
2009	204	18	8.82%
2010	185	20	10.81%
2011	254	35	13.78%
2012	204	12	5.88%
2013	157	20	12.74%
2014	229	33	14.41%
2015	209	29	13.88%
2016	135	23	17.04%
2017	184	19	10.33%
2018	247	42	17.00%
2019	229	51	22.27%

4. A review of the auditor attestations for fiscal year 2019 revealed that the most common internal control issue that led to the conclusion that ICFR were not effective was the need to make year-end adjustments.

While examining auditor attestations, analysts reviewed the disclosures for the issues that auditors indicated caused, at least in part, the conclusion that a company's ICFR was ineffective. Primarily, these reasons can be categorized as internal control (IC) deficiencies or accounting issues. A ranking of the IC deficiencies for the 2019 fiscal year end is provided on page 8 of this report, with the top five issues listed in Table 2. The most common IC reason for concluding an inadequacy of the ICFR was issues requiring year-end adjustments. The second most common reason expressed by auditors was a need for more highly trained accounting personnel.

TABLE 2

Ineffective ICFR Issues (Internal Controls)	# Attestations
Material and/or Numerous Auditor /Year-End Adjustments	133
Accounting Personnel Resources, Competency/Training	118
Information Technology, Software, Security & Access	109
Segregations of Duties/ Design of Controls (Personnel)	70
Inadequate Disclosure Controls (Timely, Accuracy, Complete)	50

5. For fiscal year 2019, the most common accounting reason for the disclosure of ineffective ICFR was revenue recognition issues.

The paragraph above focuses on IC deficiencies. In contrast, Table 3 focuses on accounting issues. As shown in Table 3, the most common accounting issue that triggered an adverse ICFR determination concerned revenue recognition issues, while the second most common accounting issue was accounts receivable and other cash issues. (*See page 9.*)

TABLE 3

Ineffective ICFR Issues (Accounting)	# Attestations
Revenue Recognition issues	66
Accounts/Loans Receivable, Investments & Cash issues	33
Liabilities, Payables, Reserves and Accrual Estimate failures	32
Tax Expense/Benefit/Deferral/Other (FAS 109) issues	29
Inventory, Vendor, and Cost of Sales issues	28

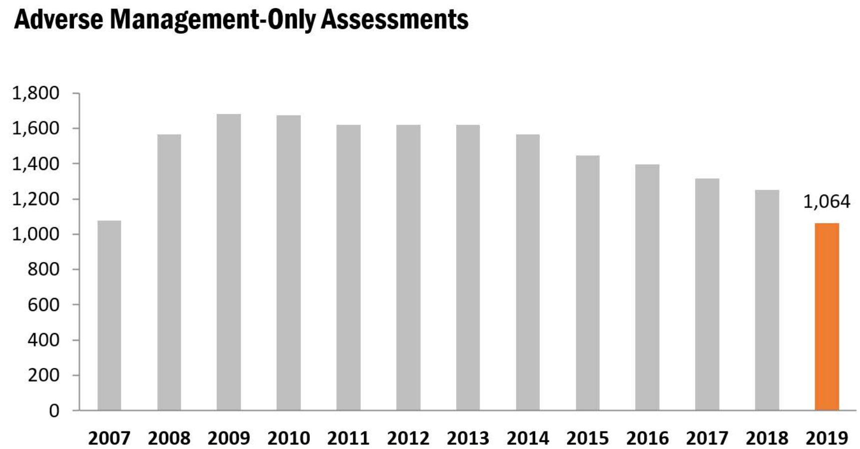
Management-Only Assessments

Non-accelerated filers that are not temporarily exempt from SOX 404 are required pursuant to subsection 404(a) to provide a management's assessment of ICFR, but are not required to file an auditor attestation (management-only assessments). Therefore, a review of companies that only file management assessments provides a focus on disclosures by smaller companies.

6. Total Number of Management-Only Assessments Disclosing Ineffective ICFR.

Non-accelerated filers were required to provide a management assessment (but not an auditor attestation) in their annual reports for the fiscal years ending on or after December 15, 2007. Figure 3 quantifies the number of management-only assessments that disclosed ineffective ICFR each year. The largest number of adverse assessments occurred during fiscal year 2009 with a total of 1,680. (*See also page 10.*) The total for 2007 was low, but high when considering that it only included companies with fiscal years ending on or after December 15th. After 2009, the number of adverse assessments dropped to 1,674 and again to 1,621. 2012 and 2013 remained virtually unchanged but were followed by six years of steady decline to a low of 1,064 in fiscal year 2019. As shown in Section 7 below, however, the steady decline does not appear when the data is shown as percentages.

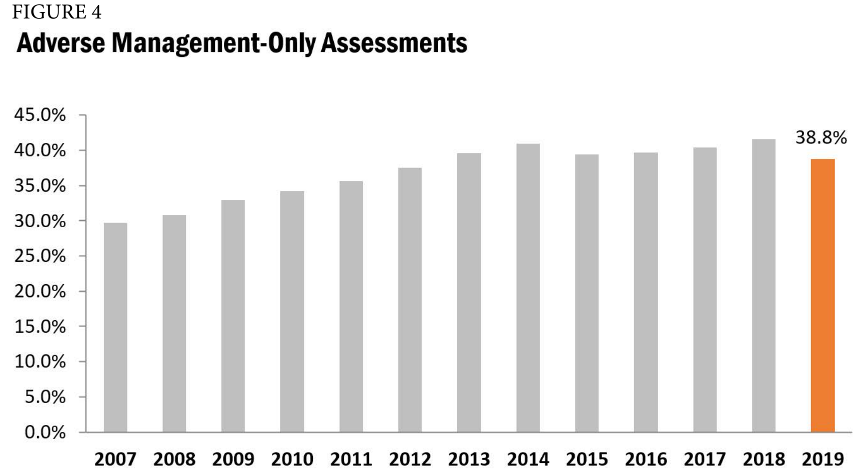
FIGURE 3



7. Total Percentage of Management-Only Assessments Disclosing Ineffective ICFR.

Figure 4 provides two noteworthy and immediate observations. First, historically and consistently, over 30% of small companies have ineffective ICFR. This figure is much higher than the 2016 local maximum of 6.7% disclosed by accelerated filers. In addition, and not revealed in Figure 3, the percentage of small companies that disclosed ineffective ICFR rose steadily for seven consecutive years from 2008 to 2014. The first improvement did not occur until fiscal year 2015, with a drop from 40.9% to 39.4%. The three years thereafter, however, saw little change when percentages remained between 39% and 40% despite the steady decline in total negative disclosures displayed in Figure 3.

FIGURE 4



The consistent percentages around 39% since 2013 indicate the difficulties small companies face in their efforts to install adequate financial systems and processes. In addition, a look back to Section 3 shows companies that leave this population and become accelerated filers tend to be better prepared than the non-accelerated filers as a whole.

8. A review of the management-only assessments for fiscal year 2019 revealed that the most common internal controls issue that led to ineffective ICFR concerns the competency and training of accounting personnel.

An examination of disclosures provided in management-only assessments found that the top IC reason given, in part or in whole, to support the conclusion that a company's ICFR are ineffective is the determination that the accounting personnel within the company were not adequately trained. Likewise, the second and fourth reasons concerned staffing. The second most common reason for ineffective ICFR is the lack of personnel necessary to implement proper segregation of duties. The fourth reason is a non-existent or understaffed audit committee. The third reason is inadequate disclosure controls, but that shortcoming could be caused by the lack of personnel necessary to implement such procedures.

It is no surprise that many small companies have not yet acquired adequate personnel, in number and/or talent, necessary to implement processes required to achieve effective ICFR. (*See page 11.*) The fact that staffing shortfalls are a pervasive difficulty for many smaller companies explains why the percentage of smaller companies that disclose ineffective ICFR maintains a value of about 39% or higher since 2013.

TABLE 4

Ineffective ICFR Issues (Internal Controls)	# Assessments
Accounting Personnel Resources, Competency/Training	859
Segregations of Duties/ Design of Controls (Personnel)	767
Inadequate disclosure controls (Timely, Accuracy, Complete)	298
Ineffective, Non-Existent or Understaffed Audit Committee	271
Material and/or numerous auditor /YE adjustments	202

9. For fiscal year 2019, the most common accounting reason for the disclosure of ineffective ICFR involves issues with accounts/loan receivables.

Similar to larger companies that commonly determined their ICFR is ineffective because of revenue recognition issues, smaller companies also tend to have cash issues. As shown in Table 5, the top accounting issue triggering the conclusion that ICFR was ineffective is a matter concerning accounts/loans receivable (the issue that ranked second for the larger companies). This accounting error, however, has only been identified and disclosed 69 times. (*See page 12.*) Therefore, in general, smaller companies tend to disclose deficiencies absent an identified accounting error.

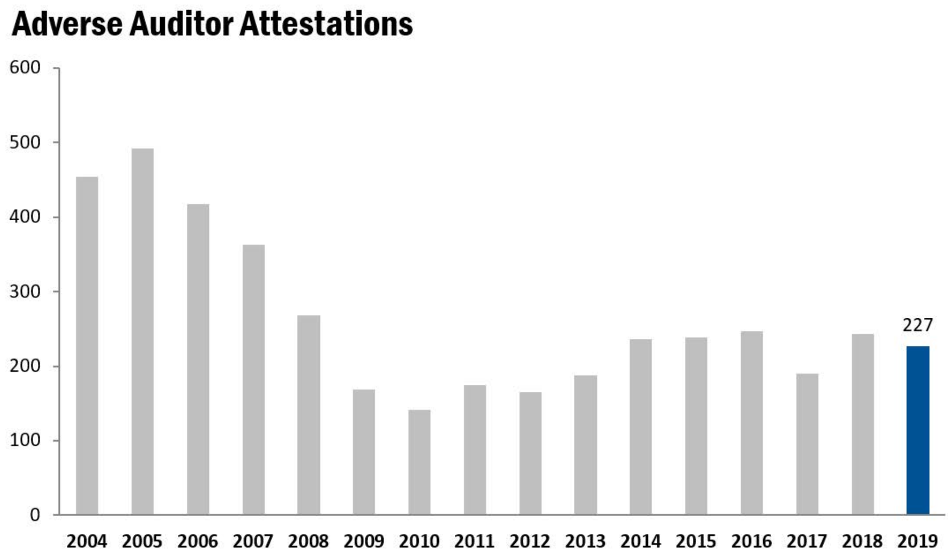
This dynamic is understandable because, for example, a company with segregation of duty problems can have ineffective ICFR while the presence of the deficiency does not demonstrate the likelihood that employees are going to wrongfully take advantage of the weakness.

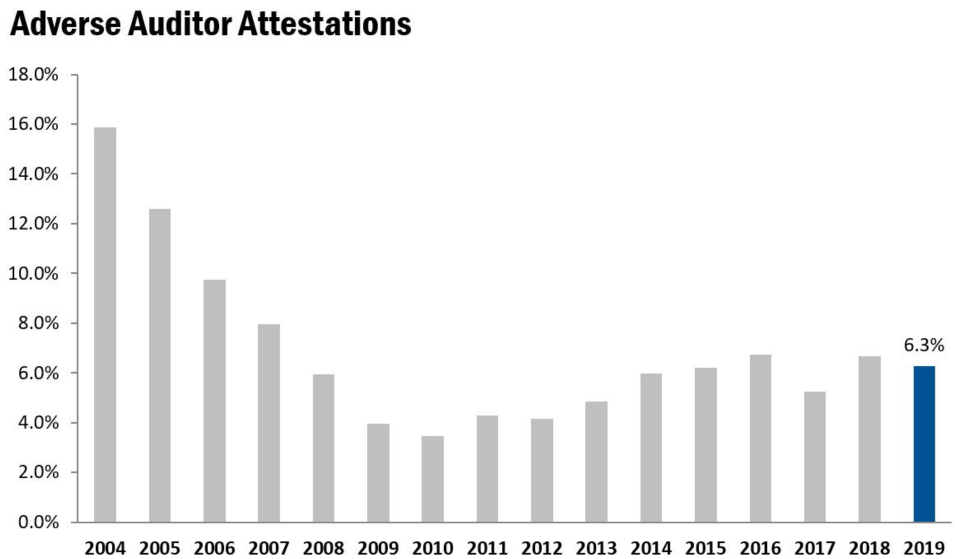
TABLE 5

Ineffective ICFR Issues (Accounting)	# Assessments
Accounts/Loans Receivable, Investments & Cash issues	69
Foreign, Related Party, Affiliated and/or Subsidiary issues	57
Revenue Recognition issues	48
Tax Expense/Benefit/Deferral/Other (FAS 109) issues	38
Liabilities, Payables, Reserves and Accrual Estimate failures	37

SIXTEEN YEAR REVIEW OF SOX 404 AUDITOR ATTESTATIONS

Ineffective ICFR Disclosures





SOX 404 Auditor Attestations

Fiscal Year	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Ineffective ICFR	454	492	417	363	268	169	141	174	165	188	236	239	247	190	243	227
Total Auditor Attestation	2,859	3,905	4,279	4,554	4,518	4,270	4,059	4,070	3,956	3,879	3,945	3,860	3,660	3,622	3,645	3,616
% of All Disclosures	15.9%	12.6%	9.7%	8.0%	5.9%	4.0%	3.5%	4.3%	4.2%	4.8%	6.0%	6.2%	6.7%	5.2%	6.7%	6.3%

Notes:

1) The research is based on a database download of July 15, 2020.
2) United States accelerated filers were first required to provide SOX 404 certifications in annual reports for fiscal years ending on or after November 15, 2004. Therefore, fiscal year 2004 covers only a partial population. Foreign companies were required to adhere to SOX 404 months thereafter. Large accelerated foreign filers were required to file auditor attestations in annual reports for the fiscal year ending on or after July 15, 2006. An accelerated foreign filer that was not a large accelerated foreign filer, however, was not required to do so until the following year. (Fore more information, see report section on page 2 titled SOX 404 Requirements History: The Staggered and Two-Tiered Implementation of SOX 404.)

AUDITOR ATTESTATIONS

Internal Control Issues Undermining Effectiveness of ICFR (Fiscal Year 2019)

Ineffective ICFR Issues (Internal Controls)	# of Ineffective Attestations	% of Ineffective Attestations
Material and/or Numerous Auditor/Year-End Adjustments	133	61.29%
Accounting Personnel Resources, Competency/Training	118	54.38%
Information Technology, Software, Security & Access issues	109	50.23%
Segregations of Duties/Design of Controls (Personnel)	70	32.26%
Inadequate Disclosure Controls (Timely, Accuracy, Complete)	50	23.04%
Journal Entry Control issues	21	9.68%
Non-Routine Transaction Control issues	17	7.83%
Restatement or Nonreliance of Company Filings	15	6.91%
Senior Management Competency, Tone, Reliability issues	8	3.69%
Restatement of Previous 404 disclosures	7	3.23%
Treasury Control issues	5	2.30%
Insufficient or Non-Existent Internal Audit Function	3	1.38%
Ineffective, Non-Existent or Understaffed Audit Committee	1	0.46%
Ethical or Compliance Issues with Personnel	0	0.00%
Ineffective Regulatory Compliance issues	0	0.00%
Management/Board/Audit Committee Investigation(s)	0	0.00%
Scope (Disclaimer of Opinion) or Other Limitations	0	0.00%
SEC or Other Regulatory Investigations and/or Inquiries	0	0.00%

Notes:

1) *The research is based on a database download of July 15, 2020.*
2) *The data above is based on 227 ineffective attestations (see page 7) out of a total of 3,616 attestations filed for fiscal year 2019.*
3) *This table does not include the generic category of "Accounting documentation, policy and/or procedures" or the relic category "SAB 108 adjustments noted."*

AUDITOR ATTESTATIONS

Accounting Issues Undermining Effectiveness of ICFR (Fiscal Year 2019)

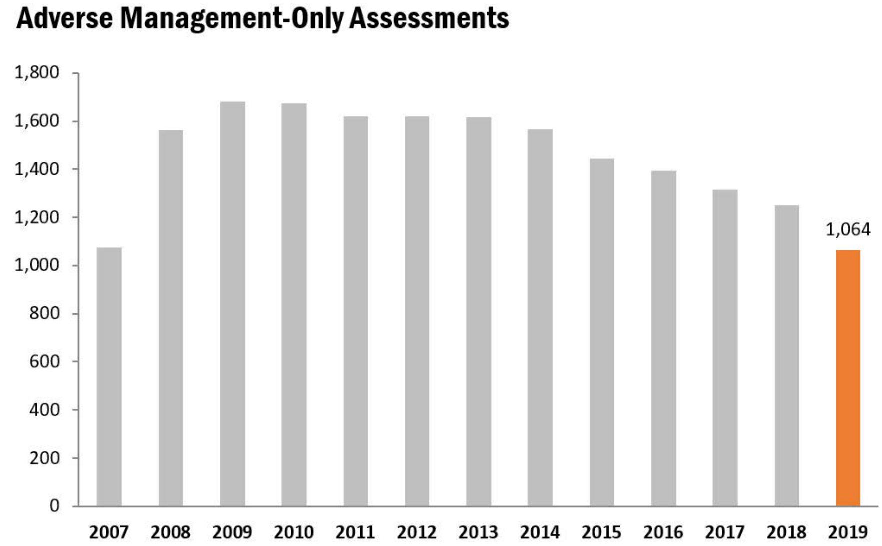
Ineffective ICFR Issues (Accounting)	# of Ineffective Attestations	% of Ineffective Attestations
Revenue Recognition issues	66	30.41%
Accounts/Loans Receivable, Investments & Cash issues	33	15.21%
Liabilities, Payables, Reserves and Accrual Estimate failures	32	14.75%
Tax Expense/Benefit/Deferral/Other (FAS 109) issues	29	13.36%
Inventory, Vendor, and Cost of Sales issues	28	12.90%
Expense Recording (Payroll, SG&A) issues	24	11.06%
Foreign, Related Party, Affiliated and/or Subsidiary issues	22	10.14%
PPE, Intangible or Fixed Asset (Value/Diminution)	19	8.76%
Lease, FAS 5, Legal, Contingency & Commit issues	15	6.91%
Lease, Leasehold & FAS 13 (98) (subcategory) issue	10	4.61%
Acquisition, Merger, Disposal or Reorganization issues	8	3.69%
Deferred, Stock-Based or Executive Comp issues	8	3.69%
Debt, Quasi-Debt, Warrants & Equity (BCF) security	7	3.23%
Depreciation, Depletion or Amortization issues	7	3.23%
Cash Flow Statement (FAS 95) Classification errors	5	2.30%
Consolidation, (Fin46r/Off BS) & Foreign Currency Translation issues	5	2.30%
Intercompany/Investment w/ Subsidiary/Affiliate	5	2.30%
Capitalization of Expenditures issues	3	1.38%
Fin Stmt, Footnote, US GAAP Conversion, Segment Disclosure	3	1.38%
Pension and Other Post-Retirement Benefit issues	2	0.92%
Balance Sheet Classification of Asset issues	1	0.46%
Debt and/or Equity Classification issues	1	0.46%
Financial Derivatives/Hedging (FAS 133) Accounting issues	1	0.46%
Income Statement Classification, Margin and EPS issues	1	0.46%
Asset Retirement Obligation issues	0	0.00%
Gain or Loss Recognition issues	0	0.00%
Loan Covenant Violations/Issues	0	0.00%

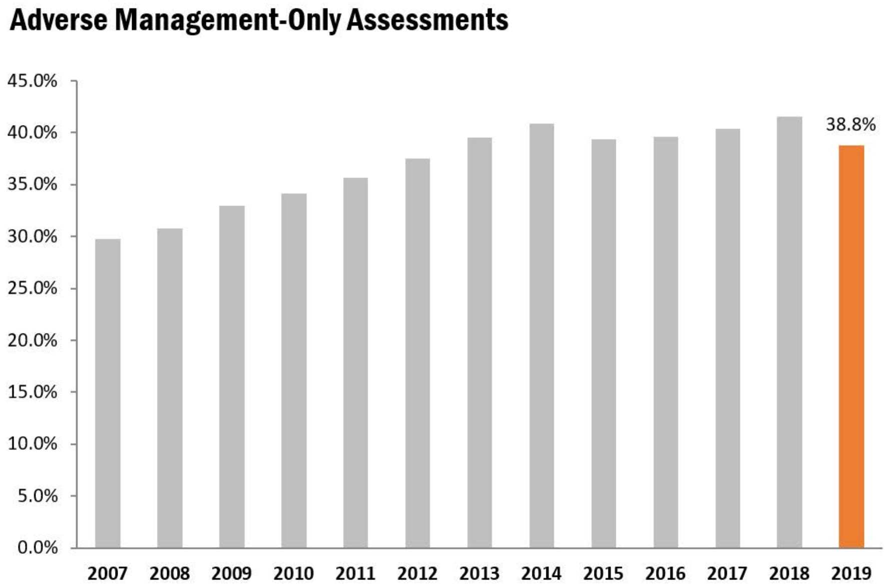
Notes:

1) *The research is based on a database download of July 15, 2020.*
2) *The data above is based on 227 ineffective attestations (see page 7) out of a total of 3,616 attestations filed for fiscal year 2019.*
3) *This table does not include the generic category of "Unspecified/unidentified/inapplicable FASB/GAAP issue."*

THIRTEEN YEAR REVIEW OF SOX 404 MANAGEMENT–ONLY ASSESSMENTS

Ineffective ICFR Disclosures





SOX 404 Management-Only Assessments

Fiscal Year	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Ineffective ICFR	1,076	1,564	1,680	1,674	1,621	1,620	1,618	1,566	1,445	1,395	1,317	1,251	1,064
Total Management-Only Assessments	3,618	5,077	5,096	4,902	4,549	4,316	4,091	3,828	3,669	3,520	3,264	3,009	2,743
% of All Disclosures	29.7%	30.8%	33.0%	34.1%	35.6%	37.5%	39.6%	40.9%	39.4%	39.6%	40.3%	41.6%	38.8%

Notes:

1) The research is based on a database download of July 28, 2020.
2) Non-accelerated filers were required to provide a management assessment (but not an auditor attestation) in their annual reports for the fiscal years ending on or after December 15, 2007. (For more information, see report section on page 2 titled SOX 404 Requirements History: The Staggered and Two-Tiered Implementation of SOX 404.) Management-only assessments are from companies that only file management assessments and therefore represent the population of smaller companies.

MANAGEMENT—ONLY ASSESSMENTS

Internal Control Issues Undermining Effectiveness of ICFR (Fiscal Year 2019)

Ineffective ICFR Issues (Internal Controls)	Total # Ineffective Assessments	% of Ineffective Assessments
Accounting Personnel Resources, Competency/Training	859	75.28%
Segregations of Duties/Design of Controls (Personnel)	767	67.22%
Inadequate Disclosure Controls (Timely, Accuracy, Complete)	298	26.12%
Ineffective, Non-Existent or Understaffed Audit Committee	271	23.75%
Material and/or Numerous Auditor/Year-End Adjustments	202	17.70%
Information Technology, Software, Security & Access issue	162	14.20%
Non-Routine Transaction Control issues	79	6.92%
Treasury Control Issues	47	4.12%
Insufficient or Non-Existent Internal Audit Function	29	2.54%
Journal Entry Control issues	25	2.19%
Restatement or Nonreliance of Company Filings	25	2.19%
Ineffective Regulatory Compliance issues	9	0.79%
Senior Management Competency, Tone, Reliability issues	8	0.70%
Restatement of Previous 404 Disclosures	4	0.35%
Ethical or Compliance Issues with Personnel	0	0.00%
Management/Board/Audit Committee Investigation(s)	0	0.00%
Scope (Disclaimer of Opinion) or Other Limitations	0	0.00%
SEC or Other Regulatory Investigations and/or Inquiries	0	0.00%

Notes

1) *The research is based on a database download of July 28, 2020.*
2) *Non-accelerated filers are not required to file an auditor attestation pursuant to S0X 404(b), only a management assessment of the effectiveness of ICFR. Management-only assessments are from companies that only file management assessments and therefore represent the population of smaller companies.*
3) *The information above is based on 1,064 ineffective assessments within a total of 2,743 management-only assessments filed for fiscal year 2019.*
4) *This table does not include the generic category of "Accounting documentation, policy and/or procedures."*

MANAGEMENT—ONLY ASSESSMENTS

Accounting Issues Undermining Effectiveness of ICFR (Fiscal Year 2019)

Ineffective ICFR Issues (Accounting)	Total # Ineffective Assessments	% of Ineffective Assessments
Accounts/Loans Receivable, Investments & Cash issues	69	6.05%
Foreign, Related Aarty, Affiliated and/or Subsidiary issues	57	5.00%
Revenue Recognition issues	48	4.21%
Tax Expense/Benefit/Deferral/Other (FAS 109) issues	38	3.33%
Liabilities, Payables, Reserves and Accrual Estimate failures	37	3.24%
Debt, Quasi-Debt, Warrants & Equity (BCF) Security	34	2.98%
Expense Recording (Payroll, SG&A) issues	29	2.54%
Inventory, Vendor, and Cost of Sales issues	20	1.75%
PPE, Intangible or Fixed Asset (Value/Diminution)	18	1.58%
Deferred, Stock-Based or Executive Comp issues	13	1.14%
Consolidation, (Fin46r/Off BS) & Foreign Currency Translation issues	12	1.05%
Acquisition, Merger, Disposal or Reorganization issues	11	0.96%
Lease, FAS 5, Legal, Contingency & Commit issues	6	0.53%
Lease, Leasehold & FAS 13 (98) (subcategory) issue	5	0.44%
Capitalization of Expenditures issues	3	0.26%
Depreciation, Depletion or Amortization issues	2	0.18%
Gain or Loss Recognition issues	2	0.18%
Income Statement Classification, Margin and EPS issues	2	0.18%
Cash Flow Statement (FAS 95) Classification errors	1	0.09%
Debt and/or Equity Classification issues	1	0.09%
Fin Stmt, Footnote, US GAAP Conversion, Segment Disclosure	1	0.09%
Financial Derivatives/Hedging (FAS 133) Accounting issues	1	0.09%
Intercompany/Investment w/ Subsidiary/Affiliate	1	0.09%
Asset Retirement Obligation issues	0	0.00%
Balance Sheet Classification of Asset issues	0	0.00%
Loan Covenant Violations/Issues	0	0.00%
Pension and Other Post-Retirement Benefit issues	0	0.00%

Notes

1) The research is based on a database download of July 28, 2020.
2) Non-accelerated filers are not required to file an auditor attestation pursuant to S0X 404(b), only a management assessment of the effectiveness of ICFR. Management-only assessments are from companies that only file management assessments and therefore represent the population of smaller companies.
3) The information above is based on 1,064 ineffective assessments within a total of 2,743 management-only assessments filed for fiscal year 2019.
4) This table does not include the generic category of "Unspecified/unidentified/inapplicable FASB/GAAP issue."

INTERNAL CONTROL WEAKNESSES (SOX 404)

DEFINITIONS FOR THE INTERNAL CONTROLS OVER FINANCIAL REPORTING ISSUES

Accounting Documentation, Policy and/or Procedures
Represents material weaknesses deriving from internal control systems that do not contain adequate documentation, policies or other means of justifying account balances. These issues may also include failures to ensure that accounts are recorded based on GAAP, SAB, FASB and/or the appropriate accounting methodology are followed. They may also include failures in policies or procedures designed to gather the correct information on a timely basis or problems with the y/e close process. It also includes failures to employ proper procedures over journal entries, non-routine transactions and other common procedural failures.

Accounting Personnel Resources, Competency/Training
Consists of problems with accounting personnel resources, competency, training, experience and/or adequacy in any way. To meet these criteria, such an indication would have to be contained in the filing or in the remediation plan.

Ethical or Compliance Issues with Personnel
Consists of problems with personnel in the areas of compliance with policies, maintenance of ethical standards, fraud and intentional acts that lead to (or could lead to) misstated account balances or financial reports.

Inadequate Disclosure Controls (Timely, Accuracy, Complete)
Represents material weaknesses related to the adequacy of information flow that should result in a required disclosure.

Ineffective or Understaffed Audit Committee
Represents circumstances where an audit committee may not have the personnel, expert, experience and/or resources to perform their duties to the extent required by Sarbanes-Oxley or their charter.

Ineffective Regulatory Compliance Issues
Consists of internal control deficiencies associated with failures to meet regulatory requirements other than taxes.

Information Technology, Software, Security & Access Issue
Deficiencies in this category include deficient program controls, software programs/implementation, segregation of duties associated with personnel having access to computer accounting or financial reporting records and related problems with oversight/access to electronic data/programs.

Insufficient or Non-Existent Internal Audit Function
Indicates circumstances where a company has stated that its internal audit function was insufficient in identifying and/or advising in the correction of internal control deficiencies. It cannot also identify circumstances where a registrant has identified a failure to have an internal audit department at all, as a ICFR failure.

Journal Entry Control Issues
This category is checked whenever the description given by the audit firm or company refers to deficiencies or issues associated with the journal entry process. This category is not checked when there is a journal entry error that originates from control deficiencies in other areas.

Management/Board/Audit Committee Investigation(s)
Consists of internal control reports indicating that an internal investigation is underway relative to accounting and/or financial reporting matters. This item is demographic in nature.

Material and/or Numerous Auditor/YE Adjustments
Represents circumstances where one of the explanations for a material weakness opinion was the number and/or size of year end adjustments including those proposed by the auditor. These adjustments also consider footnote and related errors that need to be corrected by the auditor at year-end. Too many, or auditor initiated year-end adjustments are considered prima facie evidence of a potential material weakness in financial reporting.

INTERNAL CONTROL WEAKNESSES (SOX 404)

DEFINITIONS FOR THE INTERNAL CONTROLS OVER FINANCIAL REPORTING ISSUES

Non-Routine Transaction Control Issues

This category is checked whenever a registrant specifically describes one of their control deficiencies as emanating from non-routine types of transactions. These could include acquisitions, asset sales, establishment of new systems and other.

Remediation of Material Weakness Identified

Refers to disclosures that indicate that material weakness or internal control weaknesses have been remediated.

Restatement or Nonreliance of Company Filings

Consists of material weakness opinions deriving from problems that led to restatements. Restatements are often evidentiary of primi-facie internal control deficiencies.

Restatement of Previous 404 Disclosures

Represents circumstances where a company has had to restate its 404 opinion because of some event (most likely a restatement of financials) that has occurred subsequently to filing.

SAB 108 Adjustments Noted

This item is checked when the ICFR disclosure identifies that a SAB 108, as opposed to a financial restatement, process is used to correct the beginning retained earnings balances associated with previous period accounting errors.

Scope (Resource, Time, Inclination) Limitations

A material weakness opinion may derive from assertions from the company or auditor that the company had not completed its own review of internal controls and therefore these controls could not be audited. These limitations could come about for any number of reasons.

SEC or Other Regulatory Investigations and/or Inquiries

An SEC or related investigation into the company affairs is often evidentiary of accounting or financial reporting issues that point to internal control deficiencies. This category seeks to identify circumstances where registrants have indicated in their 404 assertion that an SEC investigation or inquiry is underway.

Segregations of Duties/Design of Controls (Personnel)

This category covers internal control deficiencies associated with the design and use of personnel within an organization. It primarily deals with segregation of duty issues, such as clerks having access to both the cash receipts and the bank reconciliation. It may also deal with more sophisticated design of control issues relating to executives having the ability to change customer records, etc.

Senior Management Competency, Tone, Reliability Issues

This category has been established to identify circumstances where internal control weaknesses are attributed directly to potentially improper or negligent conduct of the current or former senior management of the company. This does not necessarily mean that the assertion is correct, just that such language exists in the filing.

Untimely or Inadequate Account Reconciliations

In reviewing internal control assertions or opinions it is often the case that inadequate account reconciliations are identified as the reason for material or numerous adjustments. This category seeks to specifically identify such circumstances.

INTERNAL CONTROL WEAKNESSES (SOX 404)

DEFINITIONS FOR THE GAAP/ACCOUNTING AREAS OF FAILURE

Accounts/Loans Receivable, Investments & Cash Issues

Consists of internal control deficiencies in approach, theory or calculations with respect to cash, cash equivalents, accounts receivable, short term investments, certain long term investments, notes, loans collectible, allowance for uncollectables, notes receivables and/or related reserves.

Acquisition, Merger, Disposal or Reorganization Issues

Consists primarily of internal control deficiencies in approach, theory or calculation associated with the merger, acquisitions, reorganization or disposal issues for registrants. The internal control issues in this area can vary from incorrect application of GAAP to calculate the proper intangible assets levels associated with acquisitions to failure to record the proper reserves for disposal or reorganization. Accounting rules in this area are considered complex and non-routine. This category is often attributed to failures by personnel in understanding certain issues associated with acquisitions or disposals.

Balance Sheet Classification of Asset Issues

Consists of internal control deficiencies in approach, theory or calculation associated with how assets were classified on the balance sheet. Primarily this category is made up of misclassified assets as short term versus long term or whether certain assets were properly considered cash equivalents versus short-term investments.

Capitalization of Expenditures Issues

Consists of internal control deficiencies in approach, theory or calculation associated with the capitalization of expenditures. These can include expenditures capitalized for inventory, construction, intangible asset, R&D, software or product development and other purposes. Whether capitalizing expenditures in inventory, leaseholds, buildings or product/software development, the proper methodology can be difficult and demanding on an internal control system.

Cash Flow Statement Classification Errors

Consists of internal control deficiencies in approach, theory or calculation that manifested themselves in cash flow statements that are not consistent with GAAP. These misclassifications can affect cash flow from operations, financing, investment, non-cash and other areas. Difficulties with respect to internal control systems over proper disclosure associated with cash flow statements typically occur with non-routine transactions.

Consolidation, (Fin46r/Off BS) & Foreign Currency Translation Issues

Consists of internal control deficiencies in approach, theory or calculation with respect to the consolidation of subsidiaries including variable interest entities and off balance sheet arrangements. This can include mistakes in how joint ventures, off balance sheet entities were recorded or disclosed. This category also identifies issues associated with foreign currency translations, minority interests, eliminations or other issues associated with consolidations.

Debt and/or Equity Classification Issues

Consists mainly of internal control deficiencies in approach, theory or calculation associated with the proper classification of debt instruments as short term or long term. This area can also refer to reclassifications between equity and debt accounts or within equity accounts.

Debt, Quasi-Debt Securities or Equity Accounting Issues

Consists of internal control deficiencies in approach, theory or calculation associated with the recording of financing/bank/securities debt or equity section accounts. Control issues in this area often arise because of incorrect recording of beneficial conversion features in debt/quasi-debt or equity securities. They can also occur with the calculation of premiums/discounts on debt securities or the proper valuation of certain non-traded equity securities.

Deferred, Stock-Based or Executive Compensation Issues

Consists of internal control deficiencies in approach, theory or calculation associated with the recording of deferred or executive compensation. The majority of these errors are associated with the valuation of options or similar derivative securities and their recording on the books. Sometimes this issue arises when personnel are paid with shares or options instead of cash. This category also includes other forms of internal control deficiencies associated with executive compensation arrangements.

INTERNAL CONTROL WEAKNESSES (SOX 404)

DEFINITIONS FOR THE GAAP/ACCOUNTING AREAS OF FAILURE

Depreciation, Depletion or Amortization Issues

Consists of internal control deficiencies in approach, theory or calculation associated with depreciation of assets, amortization of assets and/or amortization of debt premiums or discounts. This category can also include deficiencies associated with depletion of reserves or amortization of other fixed assets.

Expense Recording (Payroll, SGA) Issues

Consists of internal control deficiencies in approach, theory or calculation associated with the expensing of assets or understatement of liabilities. These issues can arise from any number areas including failure to record certain expenses, write off certain assets or acknowledge certain liabilities. This category is used primarily for miscellaneous occurrences of expensible items including payroll and SGA issues.

Financial Statement/ Footnote/ US GAAP, Segment Disclosure Issues

This represents failures or inadequacies in internal controls related to review of preparation of financial statements, footnotes and/or related additions to financial statements. This can also include issues with conversion of foreign company financial statements to US SEC/FASB Standards. It also includes internal control deficiencies associated with segment recording and related annual report disclosures.

Financial Derivatives/Hedging (FAS 133) Accounting Issues

Consists of internal control deficiencies in approach, theory or calculation of derivative instruments. These can include the valuation of financial instruments such as hedges on currency swings, interest rate swaps, purchases of foreign goods, guarantees and other. Often this category is checked when registrants fail to follow the FAS 133 rules for proper documentation or application of its principles.

Foreign, Related Party, Affiliated and/or Subsidiary Issues

Consists primarily of internal control deficiencies associated with disclosures about related, alliance, affiliated and/or subsidiary entities. This can also refer to accounting issues detected at foreign subsidiaries. This box is checked mostly in conjunction with other categories to indicate that an issue has been raised in association with a failure at a subsidiary (often foreign sub) that has been deemed to be material to the overall financial condition of the company.

Gain or Loss Recognition Issues

Consists of internal control deficiencies in approach, theory or calculation with respect to the recording of gains or losses from the sales of assets, interests, entities or liabilities. Mistakes in these areas often result from problems with calculating the proper basis for disposing of an asset or the proper amount to record as sales revenue. Generally, this category relates to issues associated with non-routine or significant transactions.

Income Statement Classification, Margin and EPS Issues

Consists primarily of internal control deficiencies associated with a registrants disclosure of financial/operational ratios or margins and earnings per share calculation issues. Also included are circumstances where income statement items are misclassified between say gross margin and selling general and administrative expenses. This may also deal with issues associated with exceptional items.

Intercompany/Investment with Sub/Affiliate Issues

Consists primarily of internal control deficiencies in approach, theory or calculation related to intercompany or affiliate balances, investment valuations or transactions. It is often the case that problems arise when intercompany balances are not reconciled and accounted for on a timely basis.

Inventory, Vendor and Cost of Sales Issues

Consists of internal control deficiencies in approach, theory or calculation associated with transactions affecting inventory, vendor relationships (including rebates) and/or cost of sales. The proper recording of inventory can be a complex area of accounting requiring many estimates. The issues can range from simple valuation calculations to estimates of completion on construction projects.

INTERNAL CONTROL WEAKNESSES (SOX 404)

DEFINITIONS FOR THE GAAP/ACCOUNTING AREAS OF FAILURE

Lease, FAS 5, Legal, Contingency & Commitment Issues

Consists primarily of internal control deficiencies associated with FAS 5 type contingencies and commitments. This description also deals with issues associated with the disclosure or accrual of legal exposures by registrants and issues associated leases and lease commitments. One significant area of impact has been internal control deficiencies associated with determining the proper accounting or determination of operating vs. capitalized leases.

Lease, Leasehold & FAS 13 (98) (Subcategory) Issues

The category is checked when a lease, leasehold or related issue has been identified with internal or financial reporting controls. This represents a subcategory of the Lease, FAS 5 category.

Liabilities, Payables, Reserves and Accrual Est Failures

Consists of internal control deficiencies associated with the accrual or identification of liabilities on the balance sheet. These could range from failures to record pension obligations, to problems with establishing the correct amount of payables, accruals or other reserves. From an internal control perspective, issues in this area most often occur because of cut-off failures in recording liabilities and matching them to related revenue or inventory accounts.

PPE, intangible or fixed asset (value/diminution) issues

Consists of internal control deficiencies in calculation, approach or theory that have taken place in the recording of PPE, fixed, intangible, goodwill or long term assets. It also applies to contra liabilities that are required to be valued or assessed for diminution. Generally issues associated with long term development projects and goodwill associated with acquisitions are included in this category.

Revenue recognition issues

Consists of internal control deficiencies in approach, understanding or calculation associated with the recognition of revenue. Many of these restatements originate from a failure to properly interpret sales contracts for hidden rebates, returns, barter or resale arrangements. They can also occur because of misapplied credits or debits associated with customer accounts. This account is generally checked without regard to other accounts they impact, such as accounts receivable.

Tax expense/benefit/deferral/other (FAS 109) issues

Consists of internal control deficiencies in approach, understanding or calculation associated with various forms of tax obligations or benefits. Many of these restatements relate to foreign tax, local taxes or tax planning issues. Some deal with failures associated with sales taxes, etc. The accounts impacted can include expense, deferral or allowances. With the change in goodwill accounting, a number of issues have arisen with the failure of companies to change the level of permanent differences in their FAS 109 calculations.

Unspecified/unidentified/inapplicable FASB/GAAP issues

This flag is identified when the 404 or 302 disclosures are lacking in sufficient information to identify what accounts or areas of financial reporting are being impacted by disclosure controls or internal control deficiencies. It may also indicate that a GAAP/FASB effect is not applicable. This flag may not be checked in circumstances where a recent section 404 report or restatement can provide the missing information.

Other - Defective or unreliable acctg/reporting records

Consists of disclosures by a registrant that a scope limitation exists with respect to the company's ability to rely on accounting or internal control records. Typically no restatement is announced because the amount, if any, cannot be determined.

INTERNAL CONTROL WEAKNESSES (SOX 404)

DEFINITIONS FOR EXEMPTIONS

Acquisitions During the Past Year

One of the allowable exemptions for not issuing and opinion on internal controls is that a company has made a recent acquisition and they have not had sufficient time to review, update and/or integrate the new acquisition into their IC systems.

Equity Method Investee (Fin 46R) Issues

Because there have been significant rule changes in this area of FASB and issues exist with respect to control/influence over equity method investees, an exemption has been granted relative to certain circumstances associated with equity method investees.

AUDIT, REGULATORY AND DISCLOSURE INTELLIGENCE

Audit Analytics delivers comprehensive intelligence on public companies, broker dealers, Registered Investment Advisors, Single Audit Non Profits and over 1,500 accounting firms. Our data includes detailed categorizations of audit and compliance issues and is considered by many professionals to be the best primary data source for tracking and analysis of the following public company disclosures:

Sarbanes-Oxley Disclosures
- Track Section 404 internal control disclosures and Section 302 disclosure controls.

Auditor Information
- Know who is auditing whom, their fees, auditor changes, auditor opinions and more.

Financial Restatements
- Identify company restatements by type, auditor and peer group. Analyze by date, period and specific issue.

Legal Disclosures
- Search all federal litigation by auditor, company and litigation type. Know who is representing whom.

Corporate Governance
- Track director & officer changes, audit committee members, C-level executives and their biographies.

SEC Comment Letters
- An extensive collection of analyzed SEC Comment Letters back to 2004 and indexed according to a taxonomy of over 2,800 issues, rules, and regulations.

Detailed reports are easily created by issue, company, industry, auditor, fees and more. These reports are downloadable into Excel. Daily notifications via email are available for auditor changes, financial restatements, adverse internal controls & disclosure controls, late filings, going concerns and director & officer changes.

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- PCAOB Inspection Reports
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- Non-Profit Single Audits
- Registered Investment Advisers
- SEC Comment Letters
- Shareholder Activism
- Stock Transfer Agents
- Tax Footnotes

Canada Databases

- Audit Fees
- Audit Opinions
- Auditor Changes
- Auditor Engagements
- Controls
- Financial Restatements

Europe Databases

- Audit Fees
- Audit Opinions
- Auditor Changes
- Auditor Engagements & Tenure
- Financial Restatements
- Key Audit Matters (KAMs)
- Transparency Reports