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Corporate Controller & CAO Hot Topics

Accounting for Economic Uncertainty Spotlight

In the current economic climate, organizations have had to adapt their disclosures and SEC filings to accommodate evolving risk areas.

The volatile environment has left organizations unsure about the extent to which they will be impacted, while an increase in SEC comment letters has underscored the need for many organizations to gain deeper insight into risks and justify key decisions.

From an economic perspective, stock prices are down for many companies, supply chain issues persist, interest rates are high, and the economy remains volatile. Recent disruptions in the banking sector have also introduced challenges, with some organizations struggling with payroll due to deposits and lines of credit being impacted. Political shifts have also left financial leaders wary about changing SEC standards and areas of interest, particularly for matters like triggers for goodwill impairment. Other areas of heightened SEC interest include revenue recognition, non-GAAP disclosures and other disclosures around climate, cyber and crypto. Against a backdrop of increased regulatory scrutiny, many companies are disclosing more contextual information than before. Amidst all of this, organizations remain focused on securing sufficient talent to maintain stability. With this confluence of economic factors, companies or at least their finance departments are not likely to experience business as usual for the near future.

Given how closely KPMG works with many of the world's leading organizations, we have unique insights into how finance leaders are approaching these topics. Below are five areas that Corporate Controllers and CAOs are focused on in the current environment. This is not intended to be a full examination of each area - rather, it highlights some key areas that are top of mind for this audience.

SEC Scrutiny / Comment Letters

The SEC has been highly active in terms of filings, issuing more comment letters recently. Most of these comments are focused on topics like non-GAAP disclosures and other frequent areas of SEC interest, but over recent years, comments have also increased on collateral in addition to filings. This has led filers to become more detailed in their comments, supporting their qualitative analysis with more robust quantitative context. Because of this, it is important for companies to ensure they have their internal controls in order, especially when dealing with unusual situations, and to respond to comment letters promptly with thorough answers.

Revenue recognition has been a primary consideration for comment letter topics in the past, and debt versus equity and gross versus net revenue recognition are still priorities. Non-GAAP disclosures and climate-related disclosures continue to be an area of focus. Disclosures around breaches and other cyber incidents have also warranted closer examination, to ensure financial statements match other released documents. The SEC is particularly interested in all things crypto, making comments far more likely if organizations have crypto-related disclosures. It is important for investors in crypto to ensure that their exchange or custodian receives a SOC-1 report, and if not, they should speak with their auditor to strengthen their controls.

Companies are operating in an unusual and/or challenging environment (e.g., higher interest rates, etc.). To the extent that organizations undertake complex or unusual transactions, accounting for that transaction is often the priority and some companies leave the control aspects to be dealt with at a later date. Best practice is often to execute the controls over significant or unusual transactions in a timely fashion and have the internal and external testing of those controls take place before the end of the fiscal year. Further, the current environment has shone a spotlight on liquidity disclosures, even for larger, well-capitalized organizations. Taking a fresh look at those disclosures considering the current environment can be a worthwhile effort, and even in cases where the company determines not to make changes to their disclosures, contemporaneous documentation around the considerations made and factors that led to that conclusion is highly advisable.

Guidance

While organizations vary in terms of the frequency of the guidance they issue, due to the confluence of recent economic risk factors, many are finding the need to update or revise their forward-looking guidance more frequently. Often, guidance can become dated or incorrect after only a few short weeks.

Some companies have characterized 2023 as a first-half versus second-half narrative, but quarterly adjustments are becoming necessary for those with rapidly evolving risk factors (e.g., supply chain disruption). In some industries, the effect of inflation on pricing as well as costs and margins has been a particular focus area in guidance, but even outside of product and service industries uncertainty around the inflationary environment may necessitate updates depending upon a company's circumstances.

By focusing on major or recurring themes, companies can develop an MD&A strategy that incorporates risk factors on an ongoing basis, addressing the dynamic economic environment and related risks without centering earnings in a static guidance approach.

Impairment

With depressed stock prices, some companies are experiencing potential triggering events for impairment (goodwill, intangibles, or both). Even those not in this situation are considering whether purely qualitative analysis is appropriate in the current economic climate. Thorough memos on a quarterly basis outlining evaluated factors can help convey organizations' assessments of impairment triggers, but auditor interest is driving a more quantitative analysis to support these qualitative statements. To the extent a company uses additional data to support its conclusions or even moves to a different model (e.g., from step 0 to step 1), a thoughtful consideration of the process and controls is necessary. Other areas of potential impairment that may have challenges in this unique environment may include the recoverability of NOLs.

Disclosures

Recent disruptions in the banking industry caused challenges for some organizations as they filed 10K disclosures. Some treasury teams are considering diversifying their cash assets. Many organizations are adding robust disclosures around their exposure in this regard as a result of these developments.

Talent Strategies

Volatility extends to the still-unsettled labor market, where wage inflation and new employee expectations continue to challenge organizations. Uncertainty around the future talent environment for accounting professionals is top of mind for many leaders as the next generation of workers shows less interest in business, finance, and accounting fields. Concerns around the talent pipeline have organizations bolstering existing partnerships with colleges around both recruitment and curriculum content and expanding partnerships beyond traditional colleges. The profession is considering going even further downstream to attract talent at the high school level. Working with FBLA and similar programs also allow organizations to identify young talent and potentially further DE&I goals.

The emergence of ChatGPT and other AI tools could profoundly alter the way finance professionals and auditors work in the future. Such tools not only offer the potential for greater automation and freedom from repetitive tasks but could also serve as means of retention for talent that wants to work with cutting-edge technology. Many companies are also reconsidering their remote flexibility approaches as they observe much higher turnover for remote employees, making their in-office policies firmer to reinvigorate collaboration and office culture. Paradoxically, some firms are also finding that pushing employees back to the office can result in dissatisfaction and, ultimately, departures, underscoring the need for companies to strike a balance between offering flexibility and mandating returns to the office.

The current economic environment has created several challenges for financial executives. Controllers and CAOs must be vigilant in ensuring compliance with SEC regulations, responding to comment letters promptly, and maintaining robust internal controls. Leaders must also prioritize talent strategies to attract and retain top accounting professionals while exploring new ways of working that keep employees engaged and productive. By taking these steps, companies can weather the economic uncertainties and position themselves for long-term success.

Related Resources:

Corporate Controller / CAO Hot Topic: Talent Spotlight

Podcast: Economic uncertainty impacts financial reporting

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