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Main articles

SEC asks issuers and audit committees to focus on audit quality in China and the impact of the coronavirus

On February 19, the SEC issued a statement regarding their ongoing dialogue with senior leaders from the largest global public accounting firm networks on audit quality in China. The most recent discussions included the potential exposure of companies to the effects of the Coronavirus and the impact that exposure could have on financial disclosures and audit quality.

The statement notes that since the PCAOB is restricted in its inspection efforts in China, the SEC expects US audit firms to bring increased attention and resources to their internal and cross-network quality control processes over audit work performed in China. Audit committees for companies with significant operations in China should be speaking to their external auditors about their efforts to ensure audit quality in China.

The statement also notes that the effects of the coronavirus on any particular company may be difficult to assess or predict, but how companies plan and respond to the events as they develop can be important information for markets. The statement also highlighted that even companies that don’t have operations in China may be impacted by events there (e.g., through suppliers, distributors or customers). From a financial reporting standpoint, the statement highlighted the need to consider potential disclosure of subsequent events in the notes to financial statements and urged companies to work with their audit committees and auditors to ensure that their financial reporting, auditing and review processes are as robust as practicable.

Companies are likely considering the direct effects on their own operations as well as the impact on entities in their supply chain, demand in affected areas and other second order effects. In addition to subsequent events disclosures, companies are likely considering disclosures of risks and uncertainties and whether, how and
when events might impact the many judgments inherent in their financial reporting. Disclosures outside the financial statements may also be appropriate. Areas of focus might include disclosures about the business, risk factors and management’s discussion and analysis of results, liquidity and capital resources (including consideration of trends and uncertainties). As events continue to unfold, decisions in these areas will likely evolve.

Audit committees should be asking management questions related to the direct and indirect impact of the coronavirus and ensuring that financial disclosures related to this topic are appropriate given the information that the company has available.

Companies and their advisors are encouraged to contact the SEC staff regarding any need for guidance or relief. The SEC staff will continue to monitor the situation and will issue guidance as they consider necessary.

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