



*Summary of Accounting and  
Auditing Enforcement Releases  
for the Quarter Ended  
June 30, 2021*

Q 2   R E P O R T   2 0 2 1

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### *Introduction and Our Objective*

We are pleased to present you with our summary of the U.S. Securities and Exchange Commission, Division of Enforcement’s Accounting and Auditing Enforcement Releases (“AAERs”) for the quarter ended June 30, 2021.

As an independent consulting firm with financial and accounting expertise, we are committed to contributing thought leadership and relevant research regarding financial reporting matters that will assist our clients in today’s fast-paced and demanding market. This report is just one example of how we continue to fulfill this commitment.

The Division of Enforcement at the U.S. Securities and Exchange Commission (“SEC”) is a law enforcement agency established to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. As such, the actions they take and releases they issue provide useful interpretations and applications of the securities laws.

For those involved in financial reporting, SEC releases concerning civil litigation and administrative actions that are identified as related to “accounting and auditing” are of particular importance. Our objective is to summarize and report on the major items disclosed in the AAERs, while also providing useful insights that the readers of our report will find valuable.

We welcome your comments and feedback, especially requests for any additional analysis you would find helpful.

Floyd Advisory  
JULY 2021

# Highlights:

- The SEC released just seventeen AAERs in Q2 2021, a diminished figure when compared to the thirty releases in Q2 2020. Although the SEC has not commented on the reduced volumes, we expect increased activity in Q3 2021 given the SEC's historical focus of settling enforcement actions prior to their fiscal year-end.
- We report on the Under Armour, Inc. case in our Recommended Reading section. The case involves allegations regarding the use of "pull forward" sales programs and raises questions about when registrants should disclose aggressive sales initiatives. We summarize the SEC's required disclosure guidance, provide an overview of the Company's "pull forward" program, and offer key considerations for management and their advisors when assessing quarter end sales programs.
- Following a quarter with no releases classified as Violations of Books and Records, the SEC released eight AAERs this quarter that fall into this category. Notably, all eight releases relate to the violation of Exchange Act Rule 12b-25, which requires detailed explanations for late filings as well as disclosures surrounding any anticipated, significant changes in the issuer's results of operations.

## OUR PROCESS AND METHODOLOGY

*The SEC identifies and discloses accounting- and auditing-related enforcement actions from within its population of civil lawsuits brought in federal court, and its notices and orders concerning the institution and/or settlement of administrative proceedings as Accounting and Auditing Enforcement Releases. The disclosed AAERs are intended to highlight certain actions and are not meant to be a complete and exhaustive compilation of all actions that may fit into the definition above.*

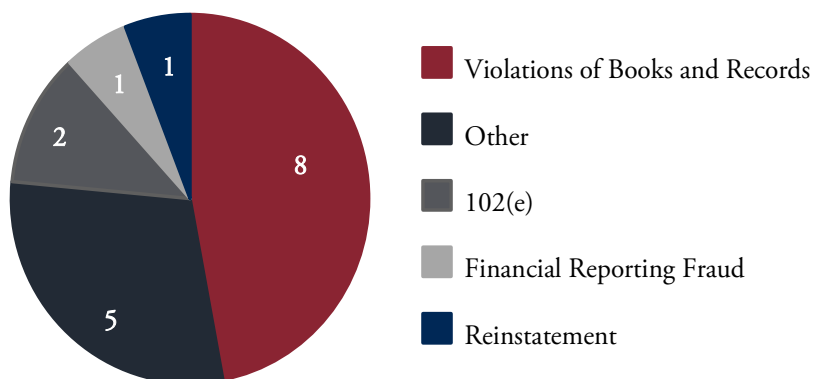
*To meet our objective of summarizing the major items reported in the AAERs, we reviewed those releases identified and disclosed by the SEC on its website, [www.sec.gov](http://www.sec.gov).*

*As part of our review, we gathered information and key facts, identified common attributes, and noted trends. Applying our professional judgment to the information provided by the SEC, we sorted the releases into major categories (i.e., Rule 102(e) Actions, Financial Reporting Frauds, Foreign Corrupt Practices Act violations ("FCPA"), Reinstatements to Appear and Practice before the SEC, Violations of Books and Records, and Other). Do note, when a release included more than one allegation, admission, or violation, we categorized the release by the most significant issue. Based on this process and methodology, we prepared a database of the key facts contained in each release.*

# The Q2 2021 AAERs: Summary by Category and Insights from the Releases

The SEC released seventeen AAERs during Q2 2021, with Violations of Books and Records actions representing nearly 50% of the total releases.

Q2 2021 AAERs by Category



"Exchange rules impose direct requirements with respect to board oversight of audits, including that boards discuss any difficult issues with the independent auditor. Likewise PCAOB rules require auditors to communicate with boards about significant issues arising in the audit."

Commissioner Allison Herren Lee  
June 28, 2021  
Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"

While our categorical breakdown is analytically useful, a closer look at specific cases for each category provides a clearer understanding of the SEC's areas of focus as an enforcement agency.

## Rule 102(e) Actions

Two AAERs were related to Rule 102(e) actions during the quarter. Rule 102(e) actions involve the temporary or permanent censure and denial of the privilege of appearing or practicing before the SEC. Summaries of the actions reported in this quarter's Rule 102(e) releases are included below:

- The SEC ordered public administrative and cease-and-desist proceedings against a CPA.*** According to the complaint, the CPA falsely claimed that its audit firm, of which he was a principal, was registered with the PCAOB. Per the complaint, the CPA falsely represented a fiscal year 2018 audit, as well as quarterly reviews for the periods ended June 30, 2018, September 30, 2018, and March 31, 2019, were conducted in compliance with PCAOB standards. The complaint further alleges the CPA failed to comply with numerous PCAOB auditing standards, including failure to properly plan the audit and identify and assess risks of material misstatement, failure to exercise due professional care and professional skepticism, and failure to prepare adequate audit documentation. The CPA agreed to reimburse the audit client for audit fees and other costs associated with the failure to register with the PCAOB in the amount of \$140,000.
- A CPA was suspended for engaging in a scheme to defraud investment advisory clients.*** The Commission's complaint alleges the co-founder and chief operating officer of an investment advisory firm in New York defrauded clients by grossly overvaluing the assets of the firm's hedge fund. The complaint alleges this individual,

a CPA, falsely reported to investors that certain fake and overvalued loan assets sold by the firm were legitimate and fairly valued. Additionally, the complaint alleges the firm had a pattern of selling overvalued or fake loans to clients for the purpose of generating liquidity and meeting various payment obligations of the fund, including redemption requests from earlier investors. Per the complaint, the CPA used mail and other mediums of interstate commerce to execute the scheme. The Commission barred the CPA from investment advisory practices and from appearing or practicing before the Commission as an accountant.

## *Violations of Books and Records*

This quarter we categorized eight AAERs under Violations of Books and Records, a category that includes alleged improper accounting treatments and internal control problems deemed worthy of an enforcement action but not meriting financial reporting fraud allegations. Below is a summary of the releases within this category.

- ***The Commission instituted cease-and-desist proceedings against eight companies for delinquent filings.*** According to the Commission's complaints, between 2019 and 2020, eight companies violated the Exchange Act Rule 12b-25, which requires issuers that fail to file periodic reports on time to submit Form 12b-25 "Notification of Late Filing" or "Form NT." Per the complaints, under Form NT, issuers are required to provide a detailed explanation as to why the company failed to file on time, as well as any anticipated, significant changes in the issuer's results of operations. As alleged in the releases, the eight companies failed to disclose in sufficient detail why they were unable to file their periodic reports on time and failed to disclose that the discovery and ongoing correction of errors in prior financial statements were among the principal reasons why they were unable to file on time. The companies were ordered to pay civil penalties amounting to either \$25,000 or \$50,000 due to these violations.

## *Reinstatement*

There was one release in Q2 2021 related to the reinstatement of a CPA.

- ***A CPA was reinstated to appear and practice before the Commission as an accountant.*** The complaint alleges the CPA engaged in improper professional conduct between 2007 and 2010. Per the complaint, the CPA's actions caused an oil and gas company to improperly inflate its earnings and materially understate its effective tax rate and tax expense through the use of deceptive intercompany tax accounting. Allegedly, the CPA failed to comply with PCAOB standards related to due professional care, professional skepticism, supervision, staffing, training, and documentation. The Commission reinstated the CPA for good cause shown.

"Investors are essentially told that if something is material, it is already being disclosed, suggesting that such disclosure is both required and effective. Even when a duty to disclose exists, however, a principles-based standard that broadly requires disclosure of 'material' information presupposes that managers, including their lawyers, accountants, and auditors, will get the materiality determination right. In fact, they often do not."

Commissioner Allison Herren Lee  
May 24, 2021  
Living in a Material World:  
Myths and Misconceptions about  
"Materiality"

# Notable Q2 2021 AAER for "Recommended Reading"

While reviewing all of the SEC's AAERs would prove insightful, certain releases present information that is especially worthy of further review and analysis by those involved with financial reporting matters. We deem these particular releases as earning the distinction of Recommended Reading for our clients and colleagues. For this quarter, we selected the following AAER to highlight.



*Accounting and Auditing Enforcement Release No. 4220 / May 3, 2021, In the Matter of Under Armour, Inc.*

*When Should Registrants Disclose Aggressive Sales Initiatives?*

Does your company use special sales programs at quarter end to meet revenue targets? Do these programs involve discounts and other special payment terms? If so, the United States Securities and Exchange Commission's recent settlement, as described in an Accounting and Auditing Enforcement Release from the SEC ("release"), with Under Armour, Inc. (the "Company"), an athletic apparel, footwear and accessories business, raises important subjects to consider regarding your financial statement disclosures.

Per the SEC, the Company's disclosures failed to describe the impact of special initiatives at quarter end to increase reported revenues and meet analysts' estimates, and the lack of proper disclosures rendered the statements misleading. Needless to say, quarter end sales initiatives occur at many companies, which is why it's important for registrants to understand the SEC's comments and consider whether there is any applicability to their sales programs.

The allegedly flawed disclosures in the Company's public filings related to the impact of what the Company termed "pull forward" sales for the third quarter of 2015 through the fourth quarter of 2016. Importantly, the term "pull forward" should be read literally as the Company incentivized customers to take shipment on orders sooner than otherwise required and did so by offering discounts and favorable payment terms.

Before discussing the information and key considerations from the release, a couple of facts worth highlighting include:

- First, there were no findings by the SEC that sales during these periods failed to comply with generally accepted accounting principles ("GAAP"),
- Second, the SEC did not file any enforcement actions against management for what are described as allegedly misleading disclosures regarding sales information and trends, and
- Finally, even with no findings of GAAP violations and no enforcement actions against management, the Company agreed to pay a civil monetary penalty of \$9 million for alleged misleading disclosures caused by the failure to describe the impact of the "pull forward" program.
- Do note, the Company neither admits nor denies any wrongdoing.

Below you will find a summary of the SEC's required disclosure guidance, an overview of the "pull forward" program, along with quotes from select emails regarding the program that were cited in the release, and considerations about the applicability of the SEC's concerns regarding whether quarter end sales efforts require special disclosures in public registrant filings.

*Management Discussion and Analysis Guidance*

The management discussion and analysis section of a registrant's public filing offers interested parties insights into management's understanding and views about the business's future opportunities and risks. Guidance for the disclosures required in this section are found in Item 303 of Regulation S-K, Management's Discussion & Analysis. Item 303(a)(3)(ii) of Regulation S-K requires that management describe, among other things,

**"As I mentioned, another means by which a duty may arise is through statements a company makes on a topic which may then require the disclosure of additional information 'necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading.' In other words, if a company makes statements on a topic, a duty may arise to disclose additional information needed to ensure that those statements are materially accurate and complete."**

Commissioner Allison Herren Lee  
May 24, 2021  
Living in a Material World:  
Myths and Misconceptions about  
"Materiality"

“any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations” in its annual report on Form 10-K.

In addition, Item 303 requires that reports describe,

“any other significant components of revenues or expenses that, in the registrant’s judgment, should be described in order to understand the registrant’s results of operations.”

Instruction 3 to Item 303(a) of Regulation S-K requires that the,

“discussion and analysis shall focus specifically on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition.”

Item 303(b) of Regulation S-K also requires discussion of material changes in such known trends or uncertainties in quarterly reports on Form 10-Q.

Per the release, and as explained below, the Company’s use of “pull forwards” created an uncertainty or event that was known to the Company’s senior management and was reasonably expected to have a material effect on the registrant’s future revenues. The failure to disclose and attribute its growth in revenue to the use of “pull forwards” therefore resulted in misleading disclosures.

## Background

Per the SEC, for six consecutive quarters from the third quarter of 2015 through the fourth quarter of 2016 (“periods under review”), the Company used “pull forwards” to help it meet analysts’ revenue estimates.

The Company reported its financial results for the periods under review in earnings calls and in periodic reports filed with the SEC. At all times, the Company described various factors underlying its consistent revenue growth, without ever disclosing that a significant portion of its revenue and revenue growth resulted from the use of “pull forwards.” In essence, the Company engaged in a continual acceleration of revenue until the market could no longer absorb the inventory.

The significance of the “pull forward” sales program was evident in the emails cited in the release including, for example, per the SEC,

- A Company senior executive acknowledged the challenges caused by the 2015 pull forwards by stating in an email: “Let’s see how of [sic] this goes and if we can get enough pull-forwards or extra business to close the Q1 gap. The issue is that we pulled forward a lot in Q4 and there is not as much room in Q2 but we will see.”
- In September 2016, the Company requested additional pull forwards from a key customer, after already having asked to move more than \$30 million in sales from the fourth quarter of 2016 to the third quarter of 2016. The customer responded by saying: “We just brought a bunch of your goods in early to help out your quarter. . . Now you want more. . . More..More..more..30% [price discount] please.” The Company ultimately agreed to a 25% price discount and an extra 30 days to pay to secure an additional \$6.7 million of pull forwards.

**“We must not operate under the false assumption that the securities laws already effectively elicit the information investors need.”**

Commissioner Allison Herren Lee  
May 24, 2021  
Living in a Material World:  
Myths and Misconceptions about  
“Materiality”

- Anticipating a revenue shortfall in the fourth quarter of 2016, in September 2016, Company senior management discussed a plan to ship a large dollar amount (ultimately over \$50 million) of orders to a new customer in December 2016, rather than in 2017 as the customer had initially contemplated. A Company senior executive acknowledged that the desire to ship the product early was being driven by pressure to meet analysts' revenue estimates, saying that the customer "isn't setting [Under Armour product in its stores] until February, so whether we thought it was \$20 or \$53 [million] or whatever, really [the customer] doesn't want any of that product in December but we are shipping it and they are absolutely taking it from us as a favor. If we were a privately held company, we would not ship that product to them in December."

Per the SEC, failing to disclose that the revenue growth being reported resulted from such aggressive sales efforts that effectively pulled sales from a subsequent period, created a misleading impression of how the Company was performing and its ability to meet or beat analysts' revenue estimates.

Internally, per the release, the Company described the "pull forward" revenue as "bad," "unnatural," and "unhealthy." Without the same information, investors did not have the ability to fully and fairly evaluate the Company's financial results and compare results across periods.

### *Considerations When Assessing Quarter End Sales Programs*

It would be naïve to deny that many companies push for sales at quarter end, or that sales pipeline reports aren't closely monitored to bring as much revenue to closure as possible to meet targets. There is nothing wrong with these efforts, and consistent with the Company's accounting, special initiatives, including discounting, can be completely acceptable under GAAP for revenue recognition.

The SEC's apparent concern, and thereby the question registrants should ask themselves is, at what point do your sales initiatives at quarter end potentially harm your ability to meet future sales expectations? The reporting requirement to discuss trends and uncertainties is certainly brought into focus when aggressive sales efforts, led by management, are nothing more than moving future sales into the current period.

The difficulty in making this assessment is estimating the point when, as mentioned above, the market can no longer absorb inventory, thereby causing an inevitable drop in future revenue. This concept is very similar to what's referred to as "channel stuffing" when pushing so much inventory into a network of distributors and resellers, that they inevitably take less product in subsequent quarters.

There are generally warning signs when special quarter end sales programs reach the problematic stage. For example, when the amount of sales required under the special initiatives is greater each quarter. This happens because the company starts each quarter with a bigger hole to fill. As also noted above, another warning sign is when customers recognize the vendor's conduct and demand greater discounts or other favorable terms to play the game. These warning signs were evident to the Company.

Every registrant's facts and circumstances will differ, so there is no bright line test for when disclosure of sales programs may be required. That said, registrants should be mindful of the goal for the management discussion and analysis section: let investors see the company through management's eyes.

"Today, investors increasingly want to understand the climate risks of issuers. Investors representing literally tens of trillions of dollars of assets under management are looking for consistent, comparable, decision-useful information to determine whether to invest, sell, or make a proxy vote one way or another."

Chair Gary Gensler  
June 23, 2021  
Prepared remarks at London City  
Week

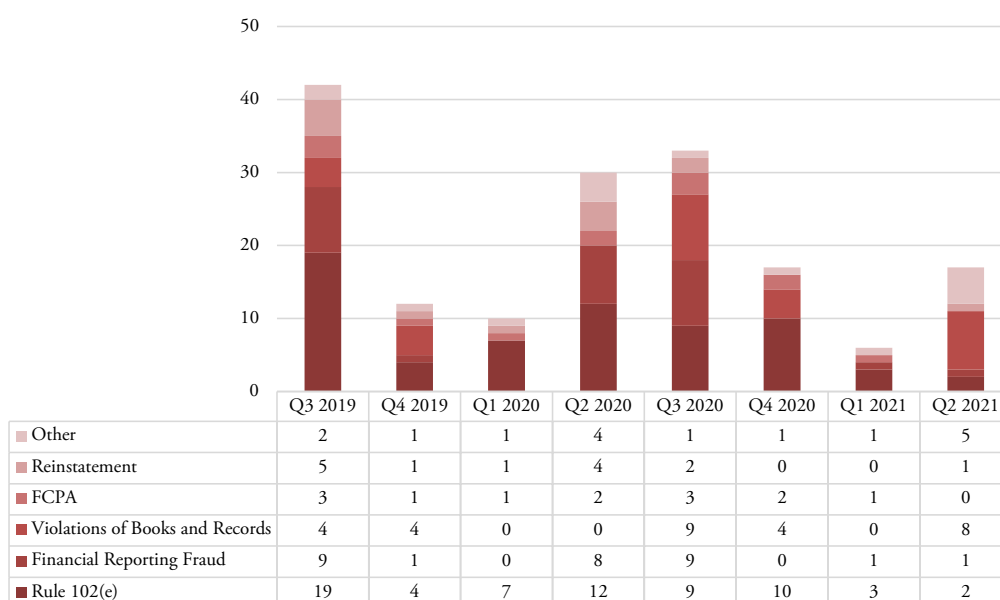


# Prior Period Comparison: Quarter to Quarter

As described in the section titled “Our Process and Methodology,” AAERs are intended to highlight certain actions and they do not represent an exhaustive and complete compilation of all actions that fit into the definitions provided by the SEC for the various AAER classifications. That said, comparisons of the number of AAERs between periods can be a useful gauge of the SEC’s activities.

The following chart maps quarterly totals for each AAER category over the past eight quarters.

Quarter to Quarter AAER Comparison  
Q3 2019 through Q2 2021



Based on this data, we made the following observations:

- While Rule 102(e) sanctions have been the most common category of release in recent periods, Violations of Books and Records and Financial Reporting Fraud sanctions combined to account for over 50% of this quarter’s releases.
- Of significance, the SEC released one AAER categorized as a reinstatement this quarter, following two quarters of no activity. It will be interesting to see whether this trend continues given the persistent Rule 102(e) suspensions over the past few years.
- The SEC released the lowest number of quarterly AAERs in over 12 years in Q1 of 2021, likely attributed, in part, to the COVID-19 pandemic. This trend appears to have continued with only 17 AAERs in Q2 2021, nearly half of the number of releases when compared to Q2 2020 results. With the SEC’s fiscal year-end approaching in Q3 2021, we are eager to observe if this trend continues.

“While we have relied on data to the degree we have data, we need to ensure that we have sufficient and accurate information to regulate effectively across the board. And in the areas I have identified, I think we need more data to ensure that the actions we take to advance the SEC’s mission – protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation – accomplish those goals.”

Commissioner Caroline A. Crenshaw  
May 14, 2021  
Mind the (Data) Gaps

[www.floydadvisory.com](http://www.floydadvisory.com)

#### **ACKNOWLEDGEMENT**

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#### **ABOUT Floyd Advisory**

Floyd Advisory is a consulting firm providing financial and accounting expertise in areas of SEC reporting, transaction advisory, investigations and compliance, litigation services, as well as business strategy and valuation.

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