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BDO USA CORPORATE GOVERNANCE PRACTICE

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AUDIT COMMITTEE DISCLOSURE RESOURCES

Audit Committees have a significant responsibility in overseeing the financial reporting process. This responsibility continues to be defined by best practices and may vary in certain aspects with respect to risk management across organizations. In the spirit of assisting audit committees with faithfully meeting this responsibility, the Center for Audit Quality (CAQ), along with various partners,¹ has established the Audit Committee Collaboration. As part of their work, a variety of tools and resources are being produced that audit committees may find of interest in strengthening their performance and improving transparency to the marketplace. The following practice aid focuses on several resources which the CAQ and others have released that specifically examine trends and emerging practices with respect to disclosures being made by public company audit committees that go beyond the immediate satisfaction of compliance expectations and provide details that may allow investors and others to gain a better understanding of audit committee performance and thought processes.

Enhancing the Audit Committee: A Call to Action: A publication issued by the Audit Committee Collaboration which serves as a call out to “public company audit committees of all sizes and industries to voluntarily and proactively improve their public disclosures to more effectively convey to investors and others the critical aspects of the important work that they currently perform.” In this regard, the Audit Committee Collaboration recognizes that the annual audit committee report included in a company's proxy statement is one of the principal sources of public audit committee-related information. Audit committees are being encouraged

¹The Center for Audit Quality (CAQ) is an autonomous, nonpartisan, nonprofit group dedicated to enhancing investor confidence and public trust in global capital markets. The CAQ has teamed up with the National Association of Corporate Directors, Corporate Board Member/NYSE Euronext, Tapestry Networks, the Director's Council, and the Association of Audit Committee Members, Inc. to form the Audit Committee Collaboration. Refer to www.auditcommitteecollaboration.org for more information.

to thoughtfully reassess their reporting and communication with stakeholders and if necessary, strengthen them going forward.

The Call to Action publication encourages audit committees to focus on the following areas:

- ▶ Clarify the scope of the audit committee's duties – in particular provide specificity regarding risk oversight
- ▶ Clearly define the audit committee's composition – provide clarity around consideration of members' qualifications and independence
- ▶ Provide relevant information about:
 - Factors considered when selecting or reappointing an audit firm – e.g., quality and qualifications of the firm such as staffing capacity, geographical reach, industry/sector experience, etc.
 - Selection of the lead audit engagement partner – information about the process and the audit committee's involvement
 - Factors considered when determining auditor compensation – disclosure of key factors on which the audit committee based its compensation decisions and the consistency with the delivery of a quality audit
 - How the committee oversees the external auditor – disclosure of the audit process and/or specific activities (e.g., number of meetings held without management's presence, types of issues discussed, and other activities)
 - The evaluation of the external auditor² - disclosure regarding the annual process and key conclusions from that evaluation

As a good practice, audit committees are encouraged to coordinate such an assessment with the full board, corporate secretary and general counsel, as well as company management and internal audit.

Click [here](#) for a recently released brief educational video promoting the Call to Action.

Audit Committee Transparency Barometer: A publication issued in December 2014 as the product of a joint research project between the CAQ and Audit Analytics, an independent research service firm, that examined 2014 audit committee disclosures in proxy statements (both the audit committee report as well as the proxy statement in its entirety) to measure the robustness of such disclosures among 1,500 companies that represented a composite of Standard & Poor's large-cap, mid-cap, and small-cap companies to establish a *baseline* reference for reporting by companies across this spectrum in future proxy seasons. In short, they concluded that across the spectrum of all size public companies, many companies are disclosing more than what is required, and many of the required disclosures are either consolidated in the audit committee report or found relatively easily within other sections of the proxy statement.

The Transparency Barometer looked at similar topics as addressed in the Call to Action outlined above and provides examples of certain disclosures of key factors whereby organizations have provided context between policies and decision-making and how such discussion may provide investors with higher confidence in the following processes and procedures that audit committees have established to carry out their role in the financial reporting process.

- ▶ **Audit firm selection:** (1) Is there discussion of the audit committee's considerations in appointing the auditor in terms of qualifications, geographic reach, or firm expertise? (2) Is there disclosure as to length of time the audit firm has been engaged?
- ▶ **Auditor compensation:** (1) Is there a discussion of audit fees and the connection to audit quality? (2) Is there a discussion of how the audit committee determines auditor compensation? (3) Is there a discussion of how non-audit services may impact independence?
- ▶ **Auditor evaluation/supervision:** (1) Is there a discussion of criteria considered when evaluating the audit firm? (2) Is there a disclosure of significant areas of the financial statements addressed with the auditor?
- ▶ **Selection of audit partner:** (1) Is it stated that the engagement partner rotates every five years? (2) Is it explicitly stated that the audit committee is involved in selection of the audit engagement partner?
- ▶ **Scope of duties:** Are key elements of the audit committee charter or other sections of the proxy included in the audit committee report (e.g., shared risk oversight)?

The questions above may be considered by all public company audit committees in their own assessments under the Call to Action in determining how robust their current disclosures are in serving the needs of the marketplace.

"Audit Committee Update: What you need to tell them, what they need to do": In April 2015, [Compliance Week](#) offered a live webinar featuring presenters from the CAQ and Audit Analytics who discussed trends and emerging issues concerning public company audit committees. The panel discussion provided a brief history of events that are currently impacting audit committees along with certain tools and resources (a few discussed above) that are available to help audit committees execute their fiduciary duties and assist them in responding to the increasing responsibilities expected of them. This included a summarization of the findings by company type (large-, mid-, small-cap) from the Audit Committee Transparency Barometer analysis.

The presenters noted the trending areas for which audit committees are being expected to show some responsibility beyond the traditional boundaries of financial reporting oversight. These other areas include the Foreign Corrupt Practices Act, risk management, and cybersecurity. In recognition of this trend, the presenters encouraged organizations toward more robust defining/delineating of the specific roles of the audit committee in contrast with those of the full board with respect to who is assuming primary oversight ("championing") of these areas. Similar advice was provided for ensuring clear definition and communication (early on and continuing throughout the audit process) of what the audit committee's expectations are with respect to the work being performed by both the internal and external auditors.

Another question raised during the presentation related to what data on assessing audit firms could be gathered and provided to audit committees and boards? Presenters agreed that readily available data

² Refer to the [CAQ's Audit Committee Essentials: The Annual Auditor Assessment](#) practice aid.

about audit fees, Securities and Exchange Commission comment letters, Public Company Accounting Oversight Board (PCAOB) and peer review inspection reports remain the prevalent data currently available for peer group comparisons but may not always be the best indicators for an organization to readily determine who the best audit firm may be to serve them. As such, the CAQ is currently piloting³ a set of Audit Quality Indicators (AQIs) in hopes of identifying metrics which could better inform stakeholders about key matters contributing to audit quality. It is anticipated the findings will be made available later in 2015. For further information, refer to the [CAQ Approach to Audit Quality Indicators](#).

The PCAOB currently has a similar but separate AQI project on its docket, whereby it is developing its own listing of AQIs to:

- ▶ Inform PCAOB regulatory processes and policy making with additional insight into the status and trends of audit quality;
- ▶ Possibly provide audit committees, investors, management, audit firms, other regulators, and the public with AQIs, providing insight into audit quality for their decisions and policy-making; and,
- ▶ Provide firms with additional incentives to compete based on audit quality.

Refer [here](#) for more information. A PCAOB AQI concept release is anticipated during 2015.

³ BDO USA, LLP, along with several of its public company audit clients, is participating in the CAQ's AQI pilot.

NEXT STEPS

Educating the public and instilling further confidence in the financial reporting process remains heavily dependent on the disclosures of the organizations about the roles, responsibilities, and activities conducted by audit committees. Beyond simply being a compliance exercise, audit committees are recognizing that the audit committee report function within the companies' proxy statement is a vehicle to provide more clear and thoughtful disclosures to promote understanding and transparency.

We encourage you to explore for yourselves the resources cited in this practice aid as you assess your own processes and disclosures. For additional audit committee tools and resources, visit the CAQ's Audit Committee Collaboration website as well as the [BDO's Corporate Governance page](#).

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