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BDO **FLASH** REPORT
CORPORATE GOVERNANCE

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SUBJECT

EVOLUTION OF VOLUNTARY AUDIT COMMITTEE DISCLOSURES

SUMMARY

As evidenced in the fourth annual Audit Committee Transparency Barometer, public companies – small through large – continue to expand voluntary disclosures within their proxy statements to provide stakeholders with further insight into oversight responsibilities, particularly with regard to the external auditor.

DETAILS

Audit Committee Transparency Barometer and Key Findings

In November 2017, the Center for Audit Quality and Audit Analytics released their fourth annual *Audit Committee Transparency Barometer*, examining the robustness of audit committee proxy disclosures among the Standard & Poor's (S&P) Composite 1500 companies. Unlike similar reports that focus on the largest public companies, this report looks at the most recent proxy statements through June 30, 2017 across small- mid-, and large-cap companies that compose the S&P 1500. The authors note that they continue to see encouraging trends with respect to voluntary, enhanced disclosure around external auditor oversight.

The *2017 Audit Committee Transparency Barometer* provides valuable data points for audit committee consideration. Areas of disclosure reviewed in the report include:

- audit firm selection
- audit firm compensation
- audit firm revaluation and supervision
- selection of engagement partner

Within each of the above noted areas, the report provides several illustrative disclosures deemed as best practices for audit committee consideration.

Key Disclosure Findings

COMPARISON		LARGE-CAP		MID-CAP		SMALL-CAP	
		2017	2014	2017	2014	2017	2014
Audit firm selection/ ratification	Audit committee considerations in appointing the external auditor	37%	13%	24%	10%	17%	8%
	Length of audit firm engagement	63%	47%	47%	42%	46%	50%
Audit firm compensation	Audit fees and its connection to audit quality	5%	13%	4%	4%	2%	1%
	How audit committee considers auditor compensation	2%	1%	1%	1%	0%	0%
	How non-audit services may impact independence	80%	83%	75%	69%	72%	58%
	Responsibility for fee negotiations	20%	8%	4%	1%	4%	1%
	Explanation of changes of fees paid to the external auditor	31%	28%	32%	30%	35%	24%
Audit firm evaluation/ supervision	Criteria considered when evaluating the external auditor	38%	8%	28%	7%	27%	15%
	Evaluation of the external auditor firm is a least an annual event	21%	4%	11%	3%	8%	4%
	Significant areas addressed with the external auditor	0%	3%	1%	2%	2%	1%
Audit engagement partner selection	Audit committee is involved in audit engagement partner selection	49%	13%	14%	1%	7%	1%
	Statement that audit partner rotates every five years	46%	16%	14%	3%	10%	4%

Within the debrief of the above findings, the CAQ and Audit Analytics highlight the belief that many audit committees who annually perform assessments of the external auditor and provide constructive feedback to the audit team may not be disclosing such activity. The CAQ points to this as a potential opportunity for audit committees to not only enhance transparency but also to underscore improvements being made to audit quality and audit quality indicators.

Mounting Pressure for Increased Disclosures?

In an era marked with increasing demand for information and complexities surrounding such, there is noted significant regulatory emphasis around disclosure coupled with rising demands by shareholders and others for more transparency around corporate governance. With the exception of the Sarbanes-Oxley Act of 2002, however, significant regulatory requirements for audit committee disclosures have not changed. In 2015, the SEC put feelers out on **possible revisions to audit committee disclosures**. Since that time, the SEC has taken a monitoring approach of developments in practice but disclosure effectiveness remains a continual theme in publicly expressed statements by SEC leadership and staff.[1]

In 2017, new Chairman of the SEC Jay Clayton **emphasized** his desire to spur capital formation and review the accessibility and meaningfulness of increasing disclosure requirements of public companies. Many have suggested that the public company audit, designed to provide investor confidence that management is accurately portraying the financial reporting for their organizations, remains somewhat of a mystery. Further, with the recent SEC **approval** of the PCAOB's new auditing standard to significantly enhance the auditor's report, audit committees are pondering whether and how this may impact company disclosures in the public filings – particularly those disclosed by the audit committee.

BDO INSIGHTS

Given complexities in transactions, increasing access to information, rapid pace of change – technology, economic, information, etc. - public demand for more transparency and understanding continues to rise. Regulators, while potentially trying to reduce an already overwhelming disclosure burden, remain focused on the balance for meaningful investor information and consideration of whether such should be mandated.

Those charged with governance can get ahead of the curve now and voluntarily incorporate more insightful disclosures in their public filings. This is a significant opportunity to provide timely and relevant information about the audit process and the related decision-making around this particular area of oversight. It further represents a means for a company to perhaps further differentiate itself from its peers and demonstrate focus on driving audit quality. The increasing illustrations highlighted in the Transparency Barometers may be a good starting point in determining where your organization currently may be positioned and how to further strengthen their disclosures in this area.

Where to Learn More?

BDO will continue to monitor developments in this area to provide timely guidance and references to our clients and contacts through our **Center for Corporate Governance and Financial Reporting**.

1 For more on SEC Disclosure Effectiveness, refer to the SEC's **website**.