



EY Center for Board Matters

# What audit committees are reporting to shareholders

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Disclosures about the vital work of public company audit committees continue to evolve. Financial reporting is at the heart of the US public capital markets, providing critical information to investors so they can make informed decisions about where to place their money. Audit committees play a key role in supporting high-quality financial reporting, including overseeing the selection, performance and compensation of the external auditor.

Despite the importance of the audit committee's role overseeing the audit, related disclosures often are limited. While an audit committee report must be included in the proxy, regulations and stock exchange listing rules require few specific disclosures about the audit and auditor. A number of companies provide voluntary disclosures regarding how audit committees exercise their audit oversight responsibilities, affording important information to investors about the reliability and quality of financial reporting.

The voluntary disclosures have shifted over time due to investor interest, market and regulatory developments, and other factors.

For more than a decade, the EY Center for Board Matters has reviewed the audit committee-related disclosures in the proxies of Fortune 100 companies to analyze their evolution. The type and scope of information has increased significantly since 2012, although the pace of change has slowed over the past several years.

## In brief

- ▶ Audit committees play an essential role in financial reporting, but disclosures about the committee's important oversight role are often limited.
- ▶ The percentage of companies providing audit committee-related disclosures has only changed slightly each year, but since 2012, we have seen notable increases.
- ▶ Companies are expanding the descriptions of audit committee oversight and responsibilities, particularly related to cybersecurity and ESG matters.

## What we saw in 2023

While the year-over-year change in the percentage of companies providing these voluntary disclosures is incremental, there has been a dramatic increase in disclosures in most categories since we began examining these disclosures in 2012. For example:

### Expansion of audit committee role

Consistent with the trends of voluntary audit committee disclosures, we continue to see companies bolster their description of audit committee oversight and the roles and responsibilities of the committee – particularly relating to cybersecurity and environmental, social and governance (ESG) matters. This responds to increased investor interest in how boards are executing their oversight of these and other nonfinancial risks (e.g., how boards are assigning oversight responsibilities at the committee level, how directors are developing related competency).

- ▶ The audit committee has emerged as the primary committee overseeing cybersecurity. Seventy-five percent of reviewed companies disclosed that the audit committee oversees cybersecurity matters. This percentage may be poised to change even further in the near future. Under Securities and Exchange Commission (SEC) finalized rules on cybersecurity, companies will need to disclose whether the entire board, specific members or a board committee is responsible for cybersecurity oversight.
- ▶ Beyond cyber, more audit committees are overseeing other nonfinancial risks or nonfinancial disclosure controls and procedures. Notably, “ESG,” “environment,” “sustainability” and “climate” are terms now appearing in the descriptions of audit committee oversight responsibilities for 29% of reviewed companies, up from 11% in 2021.

### Committee areas of focus

Leading companies are adding additional specificity by highlighting any changes to oversight activities and key focus areas for the audit committee for the previous year.

### Growing number of financial experts

We continue to see an increase in audit committees with three or more financial experts (now 68%, up from 65% in 2021 and 51% in 2012). This could be indicative of the increasing complexity of risks that audit committees are dealing with, requiring more financial expertise.

### Independence and performance of the auditor

The number of companies that disclosed factors used in the audit committee’s assessment of the external auditor’s qualifications and work quality increased to 71%, up from 68% in 2021. Only 15% of reviewed companies made that disclosure in 2012. Further, nearly 92% of companies disclosed that the audit committee considers non-audit fees and services when assessing auditor independence, vs. just 23% in 2012.

### Critical audit matters

We specifically tracked whether any of the audit committee disclosures this year referenced critical audit matters. We noted that 28% of companies made references to the audit committee’s discussion of critical audit matters with the external auditors, up from 20% in 2021.

### Auditor ratification support

In terms of voting results for proposals to ratify the auditor, support levels remain significant. In 2023, the average support was 98% for S&P 1500 companies, which is in line with recent years. Less than 1% of the auditor ratification proposals voted on in 2023 received less than 90%.

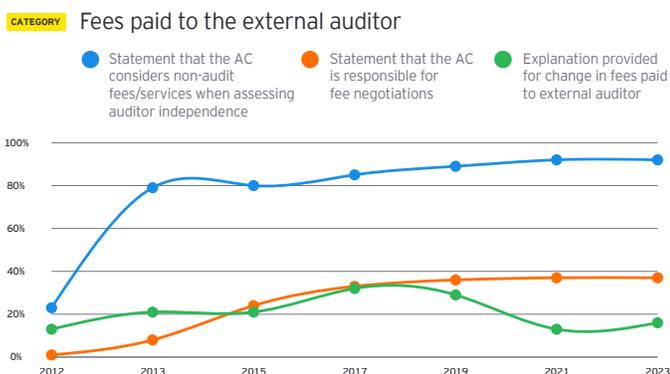
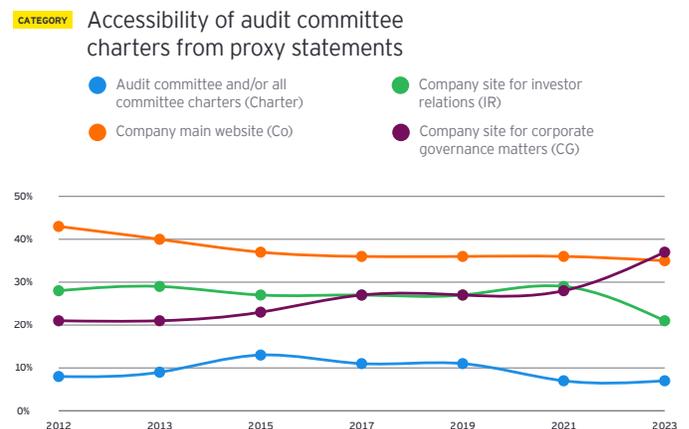
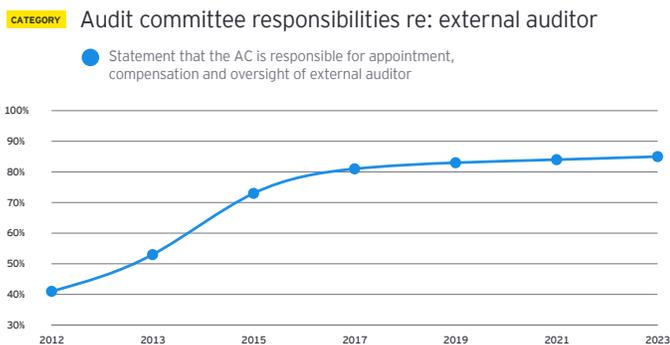
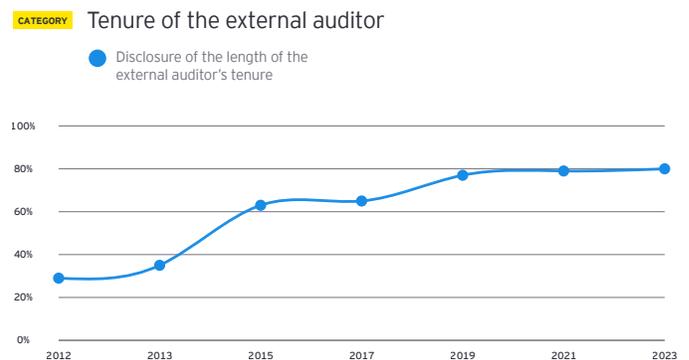
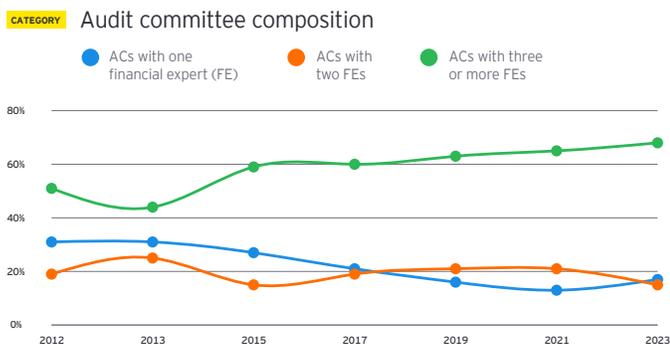
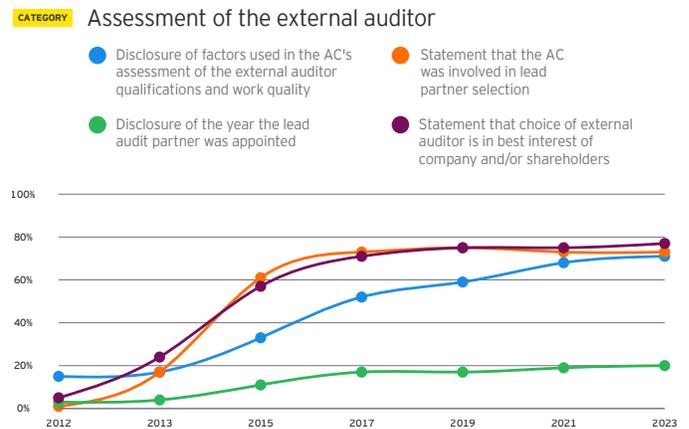
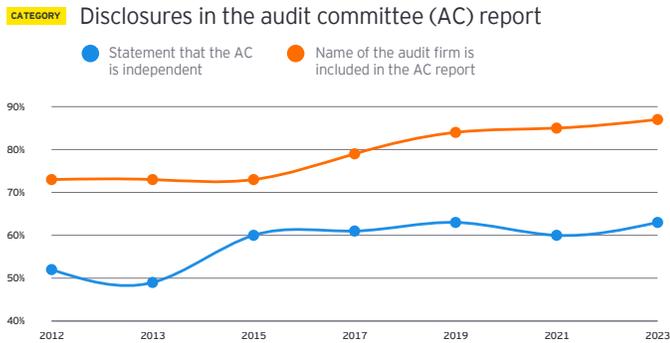
## Audit committees over time

### Audit committee composition data – S&P 500 companies

Audit committee attribute	2023	2019	2015
Size	4.3	4.2	4.2
Meetings per year	8.1	8.5	8.8
Age	63.6	63.0	63.3
Years served on board	7.2	7.7	8.2
% of designated financial experts	68%	64%	58%
% of female committee members	39%	30%	23%

# Trends in audit committee disclosures

Percentages based on total disclosures for audit committees each year. Data based on the 75 companies on the 2023 Fortune 100 list that filed proxy statements each year from 2012 to 2023.



## Disclosure observations and sample language from 2023 Fortune 100 proxy statements

### Explanation provided for a change in fees paid to the external auditor

**Most companies provide an explanation for the types of services included within each fee category. Reviewed companies explained the circumstances for the change, for example:**

*“The trend of the audit fees from 202X to 202X reflects an increase associated with Long-Duration Targeted Improvements accounting principles (approximately \$X million), offset by simplification and efficiency efforts including greater use of data and technology tools.”*

### Disclosure of factors used in the audit committee’s assessment of the external auditor’s qualifications and work quality

**Reviewed companies provided examples of criteria used in auditor assessments.**

*“As part of the Audit Committee’s annual review of Firm A and consideration to re-appoint Firm A as the Company’s independent auditor, the Audit Committee reviewed and considered, among other factors:*

Best Interest of Company X and its Shareholders	Performance	Professional Qualifications	Audit Quality	Global Capabilities	Tenure
Institutional Knowledge	Potential Impact of Changing Independent Auditor	Independence	Succession Planning	Appropriateness of Fees	External Data on Audit Quality and Performance

*In particular, the Audit Committee reviewed and considered:*

- ▶ *Whether retaining Firm A is in the best interest of the Company and its shareholders.*
- ▶ *The results of management’s assessment that includes the results of a global management survey and interviews regarding overall historic and recent performance of Firm A.*
- ▶ *The professional qualifications of Firm A and the lead audit and other senior engagement partners.*
- ▶ *The historic and current audit quality of service of Firm A and the lead audit and other senior engagement partners, including the candidness of the communications and interactions with the Audit Committee, as well as their independent judgment and professional integrity and objectivity.*
- ▶ *Firm A’s global capabilities and expertise in handling the breadth and complexity of the Company’s global operations and businesses, accounting policies and internal control over financial reporting, including Firm A’s use of technology, specialists and subject matter experts and the sharing of industry insights, trends and emerging practices.*
- ▶ *Firm A’s tenure as independent auditor, including the benefits of its institutional knowledge of the Company and its history and familiarity with the Company’s businesses, which enhances Firm A’s audit efficiency and effectiveness and provides cost efficiencies.*

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- ▶ *The potential challenges, impact and advisability of selecting a different independent auditor, including the time and expense of transitioning to a new independent auditor.*
- ▶ *Firm A's independence from the Company, noting that (i) Firm A does not provide any non-audit services to the Company other than those deemed permissible, as described under "Independent Auditor Fees", and (ii) both the Company and Firm A have controls and policies in place, including related to the applicable auditor independence rules and the mandatory rotation of the lead audit and other senior engagement partners, which helps ensure the continued independence and fresh perspectives of Firm A.*
- ▶ *Firm A's succession planning for rotation of key engagement partners.*
- ▶ *The appropriateness of Firm A's fees relative to both audit quality and efficiency.*
- ▶ *External data on audit quality and performance, including recent Public Company Accounting Oversight Board (PCAOB) reports on Firm A and peer firms."*

## Disclosure of the audit committee's involvement in lead partner selection

**Reviewed companies provide a statement noting the audit committee's involvement – some additionally provide a description of the lead partner selection process.**

*"At the Audit Committee's instruction, Firm A selects candidates to be considered for the lead engagement partner role, who are then interviewed by members of Company X's senior management. After considering the candidates recommended by Firm A, senior management makes a recommendation to the Audit Committee regarding the new lead engagement partner. After discussing the qualifications of the proposed lead engagement partner with the current lead engagement partner and senior leadership of Firm A, the members of the Audit Committee, individually and/ or as a group, interview the leading candidate."*

## Disclosure relating to the year the lead partner was selected

*"In accordance with SEC rules and Firm X policies, audit partners are subject to rotation requirements to limit the number of consecutive years of service an individual partner may provide audit services to the Firm. The lead audit partner and quality review partner may provide services to our Firm for a maximum of five consecutive years. As a result of the rotation requirements, the Audit Committee approved the selection of the current lead audit partner beginning with the 202X audit engagement. The lead audit partner is expected to serve in this capacity through the end of the 202X audit."*

## Disclosure of the audit committee's discussion of critical audit matters with its external auditor

*"In conformance with Public Company Accounting Oversight Board rules, the Committee reviewed and discussed with Firm X one critical audit matter arising from the current period audit of Company A's financial statements. Critical audit matters (CAMs) are defined to be any matter arising from the audit of the financial statements that was communicated or required to be communicated to the Audit and Risk Committee and that 1) relate to accounts or disclosures that are material to the financial statements and 2) involve especially challenging, subjective, or complex audit judgment. The Committee concurred with Firm X's assessment and identification of the CAMs contained in its Audit Report included within Company A's 202X Annual Report on Form 10-K."*

## Questions for audit committees to consider:

- ▶ Does the company's proxy statement effectively communicate how the audit committee is overseeing and engaging with the independent auditor? Does it address areas of investor interest, such as the independence and performance of the auditor and the audit committee's key areas of focus?
- ▶ How has the role of the audit committee evolved in recent years (e.g., oversight of enterprise risk management, cybersecurity risk), and to what extent are these changes being communicated to stakeholders?
- ▶ In light of the changing environment, what additional voluntary disclosures might be useful to shareholders related to the audit committee's time spent on certain activities, such as cybersecurity, data privacy, business continuity, corporate culture, and financial statement reporting developments?
- ▶ Has the audit committee considered how changes in the auditor reporting requirements may impact audit committee disclosures?
- ▶ How do director qualifications and board composition-related disclosures highlight the diversity considerations, expertise, experience and backgrounds of audit committee members?

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