

March 2015

# Point of view

Our perspective on issues of importance

## Enhancing audit committee transparency

Themes in audit committee  
disclosures in Australia, Canada,  
Singapore, the UK and the US



Building a better  
working world



## Our point of view

EY believes that greater transparency by audit committees regarding how they execute their audit oversight role can help give investors the information they need to assess the independence and effectiveness of the audit committee and the external auditor. This in turn would contribute to enhanced investor confidence, which is the foundation of strong, well-functioning capital markets globally.

## Context

Policy makers in many countries continue to consider changes to corporate governance requirements and guidance, including with regard to audit committees and their disclosures to investors. Transparent and effective audit committees help safeguard investor interests, including through their oversight of the external audit (in addition to their oversight of financial reporting and other roles). Many audit committees are providing enhanced disclosures about their work, whether in response to investor interest, good practice or changes in regulation. However, there remain significant differences in audit committee responsibilities, effectiveness and disclosures around the world.

EY reviewed audit committee-related disclosures focused on audit committees' audit oversight role in five jurisdictions – Australia, Canada, Singapore, the United Kingdom and the United States. These jurisdictions were selected due to the relative accessibility of disclosure data and the broad similarity of their legal frameworks. Each of these jurisdictions requires listed companies to have an audit committee.

This *Point of view* sets forth some key observations from EY's review. We also consider recent developments in each jurisdiction and the potential implications for future disclosures.

Our review found some common themes as well as variations in disclosures among these five jurisdictions. The most common disclosures were related to the audit committee's oversight of permitted non-audit services and auditor independence. Disclosures in this area fell in two related categories. That is, the audit committee's oversight of non-audit services provided by the auditor, and the audit committee's consideration of whether any of these services may impact the auditor's independence. The most varied disclosures were related to audit committee responsibilities and how they are executed.

While this *Point of view* focuses on disclosures related to audit committees' audit oversight role, this is only one part of most audit committees' work. The findings below should be viewed in this context. For example, while the most common disclosures from our review were related to the audit committee's oversight of non-audit services and auditor independence, in our experience this occupies only a small proportion of audit committee time.

## What we looked at

EY reviewed audit committee-related disclosures by the largest listed companies in each of the five jurisdictions.<sup>1</sup> We focused only on large listed companies to increase our ability to make comparisons across jurisdictions.

We looked at the main company document covering governance-related disclosures in each jurisdiction.<sup>2</sup> In some cases, this document refers to additional documents or the company's website for more information. These additional disclosures are not captured by our review.

EY looked specifically at the audit committee's disclosure of the following topics:

1. Key areas of audit committee focus in the past year – including new and emerging risks and industry-specific topics
2. Responsibility for the appointment, compensation and oversight of the auditor
3. Considerations in auditor selection or reappointment – including the specific factors the audit committee reviewed in selecting the auditor and/or the audit committee's assessment of auditor effectiveness
4. Oversight of the provision of non-audit services by the auditor
5. Consideration of the impact of non-audit services on auditor independence
6. Auditor tenure – disclosure of the number of years an audit firm has served as the company's auditor or the year of initial appointment

<sup>1</sup> EY reviewed the most recent available disclosures as of November 2014 for all companies in the following indices: Australia – ASX 50; Canada – TSX 60; Singapore – STI 30; UK – FTSE 100. Disclosures reviewed are for fiscal years 2013 or 2014 depending on the company's financial year-end. US findings based on *Let's talk: governance. Audit committee reporting to shareholders 2014 proxy season update*, EY, August 2014.

<sup>2</sup> Reviewed documents include: the annual report in Australia, Singapore and the United Kingdom; management information circular in Canada; and proxy statement in the United States.



## 7 key observations

### 1. Drivers of audit committee-related disclosures vary

In EY's experience, the drivers of disclosure in each jurisdiction vary. This may contribute to variation in the disclosure practices themselves. Factors that influence disclosure include:

- ▶ **Differences in regulatory and listing requirements and corporate governance guidance.** Across all the jurisdictions reviewed, there are certain regulatory and stock exchange requirements covering audit committee disclosures. These baseline requirements vary across jurisdictions. In addition, some jurisdictions have issued corporate governance best practice guidance, which also contributes to the variation we found.
- ▶ **Dual listing.** Companies listed on more than one major stock exchange often provide disclosure across a greater number of topics, reflecting compliance with multiple requirements.
- ▶ **Institutional investors.** Many companies are providing more disclosure in response to the demands of large global investors. A number of investors are seeking more information on key areas of board oversight, sometimes through public campaigns and sometimes through one-on-one engagement with companies.
- ▶ **Proxy advisory firms.** In the US and some other jurisdictions, companies are enhancing governance disclosures in response to interest from proxy advisory firms. Proxy advisors consider audit committee disclosures and company-specific audit-related matters when providing vote recommendations to their investor clients on the re-election of audit committee members and auditor ratification proposals.<sup>3</sup>
- ▶ **Directors.** Many audit committee members serve on multiple boards, sometimes across different jurisdictions, and may act as a conduit for encouraging disclosure from one jurisdiction to another.

### 2. The key areas of focus disclosed by audit committees also vary widely

Disclosure about audit committees' work over the past year, where available, often is simply a high-level summary of audit committee responsibilities, similar to what is described in an audit committee charter. However, some companies are going beyond this basic approach to provide investors with greater insight into the key areas of focus for the audit committee.

For the purposes of our review, we focused on disclosures that were explicitly about the audit committee's work in the past year and that went beyond charter-like descriptions of audit committee responsibilities.

In the UK, audit committees are now required to disclose the significant issues they considered in relation to the financial statements in the past year, and how these issues were addressed.<sup>4</sup> The most common issues disclosed in the UK relate to tax accounting, revenue recognition, valuation of goodwill, pension accounting and going concern.<sup>5</sup> In the US, audit committees are required to disclose whether they specifically discussed with the auditor certain matters in accordance with US auditing standards, such as responsibilities of the auditor in relation to the audit.<sup>6</sup> However, some US companies voluntarily disclosed additional topics discussed with the auditor, such as enterprise risk assessment, cybersecurity, compliance programs and environmental sustainability.

In other jurisdictions, some audit committees are voluntarily disclosing key focus areas. In Canada, almost half of reviewed companies disclosed key topics the audit committee worked on in the past year. Examples include information security, revisions in the audit committee charter and employee pensions. Approximately one in 10 reviewed companies in Australia and Singapore provided similar kinds of disclosure.

It is clear from our review that relatively few companies provide disclosure about the key areas the audit committee focused on in the past year. This is an area where shareholders could likely benefit from additional disclosure.

3 For example, in 2014, proxy advisory firm Institutional Shareholder Services issued a global voting recommendation policy survey on a number of topics, including whether US voting recommendation policies should examine companies' transparency with regard to audit. Investors were asked to rate the importance of disclosures, such as with regard to how the audit committee oversees the auditor and its considerations when selecting or reappointing the auditor.

4 The UK Financial Reporting Council (FRC) recently reviewed audit committee reporting by the 350 largest listed UK companies (including the 100 UK companies EY reviewed). While the FRC noted that audit committee reports generally have become more transparent and informative, it reported that one-third do not provide "good or detailed" discussion of significant accounting issues. See *Developments in Corporate Governance and Stewardship 2014*, Financial Reporting Council, January 2015. Available at: <https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Developments-in-Corporate-Governance-and-Stewardsh.pdf>

5 *Out with the old, in with the new: Observations from EY's review of December 2013 annual reports in the FTSE 350*, EY, September 2014. Available at: <http://www.ey.com/UK/en/Issues/Governance-and-reporting/EY-out-with-the-old-in-with-the-new>

6 *Audit committee reporting to shareholders: going beyond the minimum*, EY, February 2013. Available at: [http://www.ey.com/Publication/vwLUAssets/Audit\\_committee\\_reporting\\_to\\_shareholders%3A\\_going\\_beyond\\_the\\_minimum/\\$FILE/Audit\\_committee\\_reporting\\_CF0039.pdf](http://www.ey.com/Publication/vwLUAssets/Audit_committee_reporting_to_shareholders%3A_going_beyond_the_minimum/$FILE/Audit_committee_reporting_CF0039.pdf)

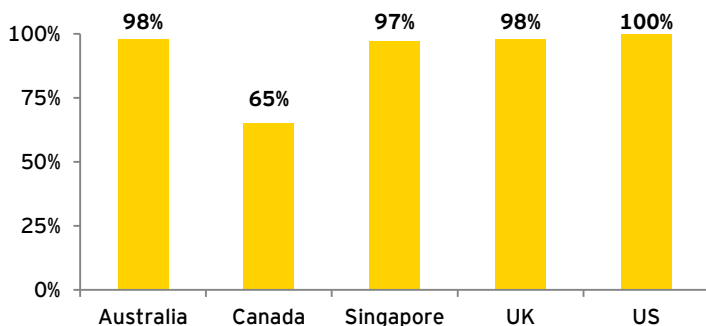
### 3. Disclosure around execution of audit committee responsibilities relating to auditor selection or reappointment is an emerging disclosure area

In each jurisdiction EY reviewed, audit committees are responsible for selecting the external auditor. However, disclosures of factors considered in auditor selection were inconsistent across the jurisdictions reviewed. In the UK, uniquely among the jurisdictions reviewed, audit committees are required to disclose annually their assessment of the effectiveness of the external audit process. This includes an assessment of the service provided by the auditor and the approach taken by the audit committee to the appointment or reappointment of the auditor.<sup>7</sup> In other jurisdictions, some audit committees voluntarily report on the rationale for auditor selection or provide examples of factors they considered when evaluating the auditor. Disclosure is lowest in Canada, where less than 10% of companies we reviewed provided such disclosure. However, this may change in response to recent guidance recommending that audit committees conduct an annual assessment of the external auditor as well as a periodic comprehensive review of the external auditor at least every five years.<sup>8</sup>

### 4. Disclosure of audit committee oversight of the provision of non-audit services by the auditor is common

The most common disclosure topic we found in our review was a statement that the audit committee's responsibilities include oversight of non-audit services. This is likely to reflect the fact that each jurisdiction has requirements or guidance covering this topic rather than the amount of time audit committees spend on it.

Nearly all companies reviewed in Australia, Singapore, the UK and US – and about two-thirds of the Canadian companies reviewed – commented on this oversight responsibility in the main investor document. Specific disclosures varied across jurisdictions. For example, many companies in Australia and Singapore simply stated that they had reviewed the non-audit services provided by the external auditor. Other companies in these jurisdictions and elsewhere described the outcome of the audit committee's non-audit services review and/or summarized the audit committee's policy on the provision of non-audit services by the external auditor.

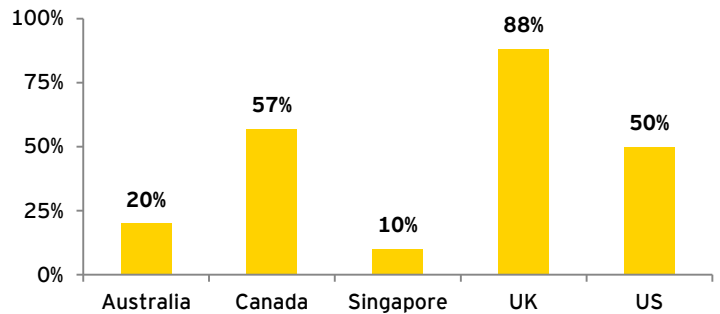


### 5. Most audit committees also disclose that they consider the impact of non-audit services on auditor independence

The second most common disclosure topic was a statement that the audit committee considered the impact of non-audit services on assessing auditor independence. Again, specific disclosures varied across markets. In most cases, they included a statement about how the audit committee monitored the auditor's independence, such as considering the specific non-audit services provided by the auditor or the level of non-audit fees paid to the auditor.

### 6. Audit committee disclosure of auditor tenure varies significantly

Between half and almost 90% of reviewed companies in the UK, US and Canada disclosed auditor tenure. In Singapore and Australia, disclosure was much lower, at 10% and 20%, respectively. Disclosure of auditor tenure increased considerably in the UK following recent revisions to the UK Corporate Governance Code. In the US, audit committees are also increasingly providing this disclosure, but on a voluntary basis, often in response to investor interest.



### 7. Audit committee-related disclosures are often dispersed throughout the main company document covering governance-related disclosures and other materials

Audit committee-related disclosures tend to be spread throughout the main company document covering governance-related disclosures and are rarely grouped in one place. For example, companies may report on the key audit committee responsibilities in several different places in a single document. The exception is in the UK, where companies are required to include a separate section in the annual report describing the work of the audit committee. In practice, audit committee-related disclosures are contained either in a dedicated audit committee report or in a subsection of the overall governance report.

<sup>7</sup> UK requirements governing audit committee disclosures are generally contained in the UK Corporate Governance Code, which operates on a "comply-or-explain" basis.

<sup>8</sup> *Oversight of the External Auditor: Guidance for Audit Committees*, Chartered Professional Accountants Canada, Canadian Public Accountability Board and Institute of Corporate Directors, January 2014

In some cases, the main company document covering governance-related disclosures refers to additional documents or to the company's website for more information on a certain topic. For example, some companies refer to additional materials for more comprehensive information about audit committee roles and responsibilities, such as the audit committee charter, documents on auditor-related policies and/or an "about us" page on the company website.

The dispersion of audit committee-related disclosures, both within the main company document covering governance-related disclosures and across other materials, can make it difficult for investors with time constraints and limited resources to gain a quick and complete understanding of an audit committee's role and responsibilities and how they are executed. The challenge increases during reporting and proxy seasons, when many of these stakeholders must evaluate and vote on a multitude of topics across hundreds or even thousands of companies.

## Looking ahead

Audit committee-related disclosures remain on the agenda for policy makers in the five jurisdictions we surveyed. Looking ahead, we expect to see the following trends continue.

### More emphasis on the audit committee's role in auditor selection and assessment

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Policy makers in Australia, Canada and the UK are publishing guidance on enhancing audit committees' role in auditor selection. We expect to see related disclosures increase as a result of this guidance.

- ▶ The Australian Securities and Investment Commission (ASIC) released a guide in 2014 for board directors on audit quality which emphasizes audit committees' role in assessing and recommending the appointment of an auditor. In our review, only 16% of reviewed Australian companies disclosed the factors considered in auditor selection, and 45% of reviewed companies disclosed that the audit committee is responsible for the appointment, compensation and oversight of the auditor. Disclosure in both these areas may increase as a result of the ASIC guide.
- ▶ In Canada, the Canadian Public Accountability Board (CPAB) and the Canadian accounting profession published guidance in 2014 for audit committees to use in their oversight of the auditor. The guidance includes a recommendation that audit committees undertake an annual assessment of the external auditor as well as a comprehensive review of the external auditor at least once every five years. The CPAB and CPA Canada have also published more detailed companion guidance for audit committees covering both reviews. Disclosure in Canada of the factors considered in auditor selection, which was the lowest among the five jurisdictions EY reviewed, is likely to increase as a result of the CPAB and CPA Canada guidance.

- ▶ In the UK, the Financial Reporting Council (FRC) recently reviewed audit committee reporting by the 350 largest listed UK companies (including the 100 UK companies EY reviewed). The FRC recognized the difficulties faced by some audit committees in relation to the required assessment of the effectiveness of the external audit process. The FRC is producing guidance to assist audit committees in discharging and reporting on this duty.

### More attention to audit committee disclosures in the US

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The US Securities and Exchange Commission (SEC) is expected to issue a concept release on audit committees in 2015 that is likely to include a focus on audit committee reporting. Among other things, SEC officials have suggested in public statements that the concept release will explore and seek comments on how to improve transparency about the role of the audit committee and its relationship with the independent auditor.

### More involvement of stock exchanges in promoting good practice and encouraging compliance

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In Australia, the Australian Stock Exchange updated its corporate governance principles in 2014, encouraging listed entities to provide an informative explanation of their governance practices including on audit committee-related matters. The updated governance principles are effective for financial years beginning on or after 1 July 2014. In Singapore, the Singapore Exchange published a disclosure guide in February 2015 aimed at aiding companies' compliance with the Code of Corporate Governance. Although the guide does not focus on audit committee-related disclosures, it emphasizes the need for companies to avoid "boilerplate" statements and provide meaningful information in their disclosures.

### Enhancements to auditor reporting may encourage enhanced audit committee-related disclosures

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Policy makers around the world have introduced or are considering enhancements to auditor reporting requirements. The International Auditing and Assurance Standards Board (IAASB) released its new auditor reporting standards in January 2015. The new standards are effective for audits of financial statements for periods ending on or after 15 December 2016. The UK and the Netherlands have already adopted elements of the new IAASB standards. The US Public Company Accounting Oversight Board (PCAOB) also is expected to move forward in 2015 with a revised proposal to enhance auditor reporting.

These developments could in turn encourage more audit committees to provide more voluntary disclosure. For example, the new IAASB standards require the auditor to identify and include in the auditor's report matters the auditor considers to be "key" to the audit. This may encourage investors and other users of audit committee disclosures to seek more information from audit committees about their key areas of focus.

## Summary table

Topics of disclosure	Average across five jurisdictions	Australia	Canada	Singapore	UK	US
1. Key areas of audit committee focus in the past year	36%	10%	48%	13%	99%	8%
2. Responsibility for the appointment, compensation and oversight of the auditor	61%	45%	53%	63%	79%	65%
3. Considerations in auditor selection or reappointment	36%	16%	8%	27%	99%	31%
4. Oversight of the provision of non-audit services by the external auditor	92%	98%	65%	97%	98%	100%
5. Consideration of the impact of non-audit services on auditor independence	81%	96%	40%	97%	94%	80%
6. Auditor tenure	45%	20%	57%	10%	88%	50%

Note: Shaded cells reflect required disclosure topics. In some cases, the percentage may be less than 100% because required disclosures may be outside the main company document aimed at investors.

## Conclusion

The findings from the five jurisdictions reviewed represent possible opportunities for audit committees to consider their own disclosures and whether they can increase the transparency about how they are carrying out their important oversight role. The findings also provide a starting point for conversations between companies, policy makers and investors on audit committee disclosures. Of course, enhanced audit committee-related disclosures are not an end in themselves. The shared goal of companies, investors and policy makers should be increased awareness among investors of the responsibilities of the audit committee and how it is executing them, leading to better alignment of interests among all stakeholders in the financial reporting chain.

## Further reading

- ▶ [EY Overview, Auditor reporting, October 2014](#)
- ▶ [Out with the old, in with the new: observations from EY's review of December 2013 annual reports in the FTSE 350, with recommendations for 2013, EY, September 2014](#)
- ▶ [Let's talk governance: audit committee reporting to shareholders 2014 proxy season update, EY, August 2014](#)
- ▶ [EY Point of view, Auditor reporting, February 2014](#)
- ▶ [EY Point of view, Enhancing transparency of the audit committee auditor oversight process, November 2012](#)



## Local disclosure requirements and guidance

### Australia

- ▶ Corporations Act 2001 (Section 300). Available at: <http://www.comlaw.gov.au/Current/C2004A00818>
- ▶ Corporate Governance Principles and Recommendations, 3<sup>rd</sup> Edition, Australian Stock Exchange Corporate Governance Council, March 2014. Available at: <http://www.asx.com.au/regulation/corporate-governance-council.htm>
- ▶ Information Sheet 196: Audit quality: The role of directors and audit committees, Australian Securities and Investment Commission, March 2014. Available at: <http://asic.gov.au/regulatory-resources/financial-reporting-and-audit/auditors/audit-quality-the-role-of-directors-and-audit-committees/>

### Canada

- ▶ Canadian provincial securities regulators require certain audit committee disclosures for listed companies:
  - ▶ National Instrument 58-101. Available at: [http://www.osc.gov.on.ca/en/SecuritiesLaw\\_rule\\_20050617\\_58-101\\_disc-corp-gov-pract.jsp](http://www.osc.gov.on.ca/en/SecuritiesLaw_rule_20050617_58-101_disc-corp-gov-pract.jsp)
  - ▶ Multilateral Instrument 52-110. Available at: [https://www.osc.gov.on.ca/documents/en/Securities-Category5/rule\\_20040326\\_52-110-audit-comm.pdf](https://www.osc.gov.on.ca/documents/en/Securities-Category5/rule_20040326_52-110-audit-comm.pdf)
- ▶ *Oversight of the External Auditor: Guidance for Audit Committees*, Chartered Professional Accountants Canada, Canadian Public Accountability Board and Institute of Corporate Directors, January 2014. Available at: [http://www.icd.ca/getmedia/ac88804a-db90-4cf5-a006-a674a944ac59/item78035\\_Guidance\\_EN.pdf.aspx](http://www.icd.ca/getmedia/ac88804a-db90-4cf5-a006-a674a944ac59/item78035_Guidance_EN.pdf.aspx)

### Singapore

- ▶ Companies Act (Chapter 50). Available online at: [https://www.acra.gov.sg/Legislation/Companies\\_Act/](https://www.acra.gov.sg/Legislation/Companies_Act/)
- ▶ SGX-ST Listing Manual (Mainboard rules), Singapore Exchange. Available at: [http://rulebook.sgx.com/en/display/display\\_main.html?rbid=3271&element\\_id=4830](http://rulebook.sgx.com/en/display/display_main.html?rbid=3271&element_id=4830)
- ▶ *Code of Corporate Governance*, Monetary Authority of Singapore, May 2012. Available at: [http://www.mas.gov.sg/~media/resource/fin\\_development/corporate\\_governance/CGCRevisedCodeofCorporateGovernance3May2012.pdf](http://www.mas.gov.sg/~media/resource/fin_development/corporate_governance/CGCRevisedCodeofCorporateGovernance3May2012.pdf)
- ▶ *Guidebook for Audit Committees in Singapore, Second Edition*, Audit Committee Guidance Committee, August 2014. Available at: [https://www.acra.gov.sg/uploadedFiles/Content/Publications/Guides/Guidebook%20for%20ACs%20\(2nd%20edition\).pdf](https://www.acra.gov.sg/uploadedFiles/Content/Publications/Guides/Guidebook%20for%20ACs%20(2nd%20edition).pdf)

### UK

- ▶ *UK Corporate Governance Code*, Financial Reporting Council, September 2014. Available at: <https://www.frc.org.uk/Our-Work/Codes-Standards/Corporate-governance/UK-Corporate-Governance-Code.aspx>
- ▶ *Guidance on Audit Committees*, Financial Reporting Council, September 2012. Available at: <https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Guidance-on-Audit-Committees-September-2012.pdf>

### US

- ▶ Securities and Exchange Commission (SEC) rules:
  - ▶ 15 USC 78j-1(h), (k), (m). Available online at: <http://www.gpo.gov/fdsys/pkg/USCODE-2010-title15/html/USCODE-2010-title15-chap2B-sec78j-1.htm>
  - ▶ 17 CFR § 229.407. Available online at: <http://www.gpo.gov/fdsys/pkg/CFR-2011-title17-vol2/pdf/CFR-2011-title17-vol2-sec229-407.pdf>
  - ▶ 17 CFR § 240.14a-101. Available online at: [http://www.ecfr.gov/cgi-bin/text-idx?SID=8e0ed509ccc65e983f9eca72ceb26753&node=17:4.0.1.1.1&rgn=div5#se17.4.240\\_114a\\_6101](http://www.ecfr.gov/cgi-bin/text-idx?SID=8e0ed509ccc65e983f9eca72ceb26753&node=17:4.0.1.1.1&rgn=div5#se17.4.240_114a_6101)
- ▶ Listing rules:
  - ▶ New York Stock Exchange rules 303A.06 and 303A.07. Available online at: <http://nysemanual.nyse.com/lcm/>
  - ▶ NASDAQ Stock Market rule 5605(c). Available online at <http://nasdaq.cchwallstreet.com/>

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