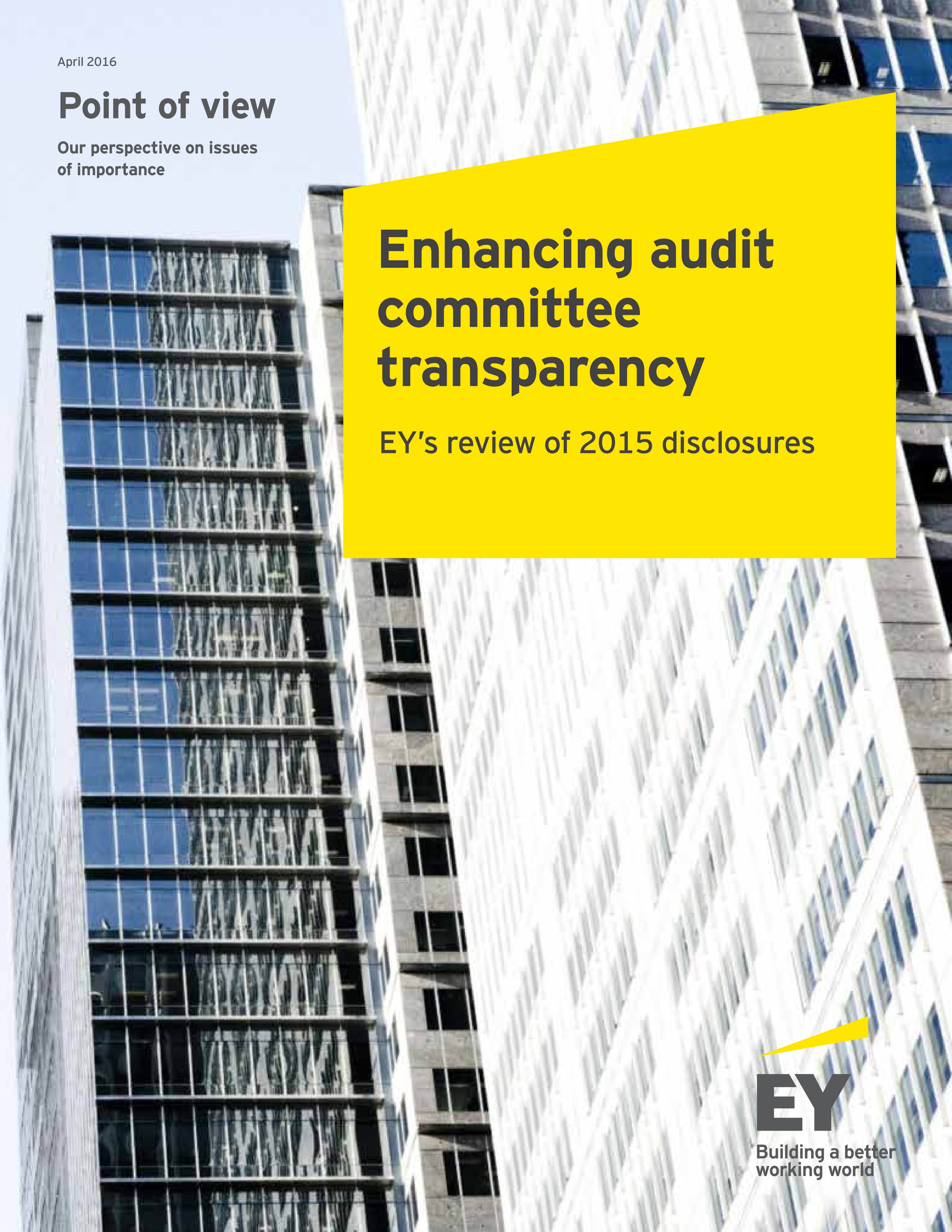


April 2016

Point of view

Our perspective on issues of importance

Enhancing audit committee transparency

EY's review of 2015 disclosures

EY

Building a better working world

Our point of view

EY believes that independent and effective audit committees contribute to investor confidence and well-functioning capital markets. To help give investors the information they need to assess the effectiveness of audit committees and the external auditor, we believe audit committees should focus on the quality of their disclosures as well as the scope.

This *Point of view* sets forth key observations from EY's study of 2015 audit committee-related disclosures with a focus on the audit committee's oversight of the external audit process in five jurisdictions — Australia, Canada, Singapore, the United Kingdom (UK) and the United States (US). It builds on our initial study, which looked at disclosures from the 2014 reporting season and was published in March 2015.[1]

Context

Policymakers in many countries continue to consider corporate governance reforms, including measures to strengthen audit committees and their disclosures. Specific developments in 2015 in the jurisdictions reviewed that affect audit committee disclosures include:

- The Australian Securities Exchange (ASX) Corporate Governance Principles now allow companies to provide corporate governance disclosures in either the annual report or the company website
- The Chartered Professional Accountants of Canada and the Canadian Public Accountability Board's "Enhancing Audit Quality" (EAQ) initiative of 2013 continues to have an impact on audit committee reporting
- The Singapore Accounting and Corporate Regulatory Authority's guidance for audit committees on the Audit Quality Indicators (AQIs) Disclosure Framework
- The UK Financial Reporting Council's guidance for audit committees in evaluating the effectiveness of the external audit process
- The US Securities and Exchange Commission's Concept Release on Possible Revisions to Audit Committee Disclosures
- The US Public Company Accounting Oversight Board's Concept Release on AQIs[2]

Consistent with these developments, we observed a modest increase in some audit committee-related disclosures in the last year. Most audit committees continue to be transparent about their fundamental responsibilities to oversee the external audit process; however, disclosures remain limited in offering insights into how those responsibilities are carried out.

1 *EY Point of view, Enhancing audit committee transparency* (March 2015). These jurisdictions were chosen due to the relative accessibility of disclosure data and the broad similarity of their legal frameworks. Each jurisdiction requires listed companies to have an audit committee.

2 *3rd edition of the ASX Corporate Governance Principles* (March 2014); Chartered Professional Accountants of Canada and CPAB "Enhancing Audit Quality" initiative (May 2013); *Guidance to Audit Committees on ACRA's Audit Quality Indicators Disclosure Framework* (October 2015); UK *FRC Audit Quality Practice Aid for Audit Committees* (May 2015); US *SEC Concept Release on Possible Revisions to Audit Committee Disclosures* (July 2015); US *PCAOB Concept Release on Audit Quality Indicators* (July 2015).

What we looked at

As with our 2015 study, EY reviewed audit committee disclosures by the largest listed companies in each of the five jurisdictions.[3] We continued to focus on large listed companies to facilitate our ability to make comparisons across jurisdictions and with the findings in our 2015 report. We again reviewed the main company document covering governance-related disclosures in each jurisdiction. In some cases, this document refers to additional sources for more information. These additional disclosures generally are not captured in our review.[4]

EY looked at 14 disclosure topics (see "Summary table"). We looked at the five topics explored in our 2015 study for the purpose of trend analysis. We also looked at disclosures relating to eight additional topics covered in an EY review of US audit committee reporting to see how the reporting of these topics compared across the other jurisdictions.[5] We also reviewed audit committee reporting of diversity, reflecting the significant stakeholder interest in board diversity in many jurisdictions.

What we found: six key observations

1. Audit committees still provide relatively few insights into how they oversee the auditor

Nearly 60% of companies we reviewed across the five jurisdictions disclose that the audit committee is responsible for the appointment, compensation and oversight of the external auditor. This is consistent with our findings from last year. By contrast, disclosures related to how the audit committee oversees the external auditor are much less common. For example, fewer than one in five companies (15%) provide a statement regarding whether the audit committee is responsible for fee negotiations, while just over a third of audit committees (37%) disclose the factors used in the audit committee's assessment of the external auditor's qualifications and work quality. Factors disclosed include value delivered to shareholders, industry experience and the quality of the engagement team.

We observed an increase in the disclosure of the factors used in the audit committee's assessment of the auditor's qualifications and work quality in Singapore (from 33% to 47%) and Canada (from 10% to 20%). In Singapore, this may be explained by the publication of revised guidance for audit committees by Singapore authorities which includes information for evaluating the external auditor.[6] In Canada, this may reflect the influence of the EAQ initiative (see "Context"). Among other things, the EAQ focused on the role of the audit committee in external audit oversight.

3 EY reviewed the most recent available disclosures as of November 2015 for all companies in the following indexes: Australia – ASX 50; Canada – TSX 60; Singapore – STI 30; UK – FTSE 100. Disclosures reviewed are for fiscal years 2014 or 2015 depending on the company's financial year-end. US findings based on *Audit committee reporting to shareholders in 2015* and covers 76 companies drawn from the Fortune 100 in 2015 that filed proxy statements for three consecutive years. Where a company is a new addition to an index this year, we also reviewed the company's previous year's disclosures to allow for a like-to-like comparison. This means that some of the percentages for 2014 quoted in this *Point of view* differ slightly from the percentages quoted in EY's earlier *Point of view*.

4 Reviewed documents include the annual report in Australia, in Singapore and in the United Kingdom; the management information circular in Canada; and the proxy statement in the United States. Given changes in disclosure-related guidance in Australia following our 2015 publication (see 3rd edition of the *ASX Corporate Governance Principles*, which now allow companies to provide corporate governance disclosures in either the annual report or the company website), we also reviewed audit committee-related disclosures contained within the company website for Australia.

5 *Audit committee reporting to shareholders in 2015*, EY Center for Board Matters (September 2015).

6 *Guidebook For Audit Committees Revised To Ensure Continued Relevance*, The Monetary Authority of Singapore (MAS), the Accounting and Corporate Regulatory Authority (ACRA) and the Singapore Exchange (SGX) (August 2014).

2. Most audit committees continue to disclose that they consider the impact of non-audit services on auditor independence

A statement that the audit committee considered the impact of non-audit services when assessing auditor independence continues to be the most common disclosure (80%) across the five jurisdictions. This may reflect the fact that each jurisdiction has requirements or guidance covering audit committee oversight of non-audit services. It also may reflect the continued focus of policymakers on the audit committee's oversight of non-audit services provided by the external auditor.

In most cases, these disclosures highlighted that the audit committee considered the specific non-audit services provided by the auditor and/or the level of non-audit fees paid to the auditor.

3. The key areas of focus disclosed by audit committees continue to vary

We looked again this year at disclosures about the audit committee's work. We found that few companies disclosed information about the topics discussed by the audit committee. Many echoed the responsibilities audit committees have under their charter.

Cybersecurity was identified as an increasing area of focus for audit committees across the five jurisdictions. Most disclosures acknowledge cybersecurity vulnerabilities and the need for the audit committee to monitor these going forward. Disclosures of other areas of focus varied across the five jurisdictions.

In the UK, audit committees are required to disclose the significant issues they considered in relation to the financial statements in the past year. Consistent with our 2015 findings, the most common issues disclosed included revenue recognition, impairment of goodwill, pension accounting and going concern. In addition, around half of UK audit committees disclosed a focus on tax issues, a small increase since last year.

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. However, some US companies voluntarily disclosed additional topics discussed with the auditor. The volume and the topics disclosed are generally the same as the 2014 reporting season, and included cybersecurity and risk compliance.

In Canada, over half of reviewed companies voluntarily disclosed key topics the audit committee considered in the past year, a small increase compared with last year. The most common topic disclosed was cybersecurity. Around 15% of companies in Australia voluntarily disclosed key topics the audit committee worked on, and these included tax and anti-corruption. We did not observe disclosure of key topics in Singapore.[7]

4. Disclosure of auditor tenure is increasing but continues to vary significantly across jurisdictions

Consistent with last year, disclosure of auditor tenure remains the highest in the UK (85%). There also has been an increase in UK audit committees disclosing when they plan to issue an audit tender. This likely reflects the active UK audit tendering environment, resulting from the introduction of mandatory audit tendering in 2012 and the pending implementation of the European Union audit legislation, due to take effect in June 2016.

Disclosure of auditor tenure also was relatively high and has increased since last year in the US (from 50% to 59%) and in Canada (from 57% to 62%). In the US, this increase may reflect continued investor interest in the topic. In Canada, the increase may reflect the fact that auditor tenure and its impact on audit quality have been discussed as part of the EAQ initiative, mentioned above.

The disclosure of auditor tenure was much lower in Australia, although it did increase slightly from last year (27% to 29%). Disclosure on this topic remained low in Singapore (3%).

7 This represents a small decrease from last year's review and reflects the fact that two companies that were listed on the Straits Times Index (STI) in 2014 are no longer listed on the 2015 index.

5. Disclosure by audit committees on why their choice of external auditor is in the best interests of the company and/or shareholders is an emerging practice

In most jurisdictions, we observed no disclosures about whether or how the choice of external auditor is in the best interests of the company and its shareholders. We found that most audit committees included a statement recommending the appointment or reappointment of the external auditor, or a statement that the audit committee was satisfied with the performance of the auditor.

In the US, however, more than half of companies provided an explicit statement that the choice of external auditor is in the best interests of the company and/or shareholders. While not a regulatory requirement in the US, the disclosure of this information has increased in the last year and is likely a response to investor interest in enhanced disclosures regarding the audit committee's oversight of the audit relationship.

6. Many audit committees disclose information related to their composition with a focus on independence and financial expertise

Because of the specific requirements placed on the composition of audit committees in many jurisdictions, we observed a significant number of audit committees disclosing the independence (75%) and financial expertise (75%) of their members. It is less common for audit committees to disclose other aspects of their composition, including industry expertise (11%) and diversity (negligible).

While our review focused on audit committee-related disclosures, we found that where information about industry expertise and diversity is disclosed, this is typically done on a boardwide rather than committee-specific basis:

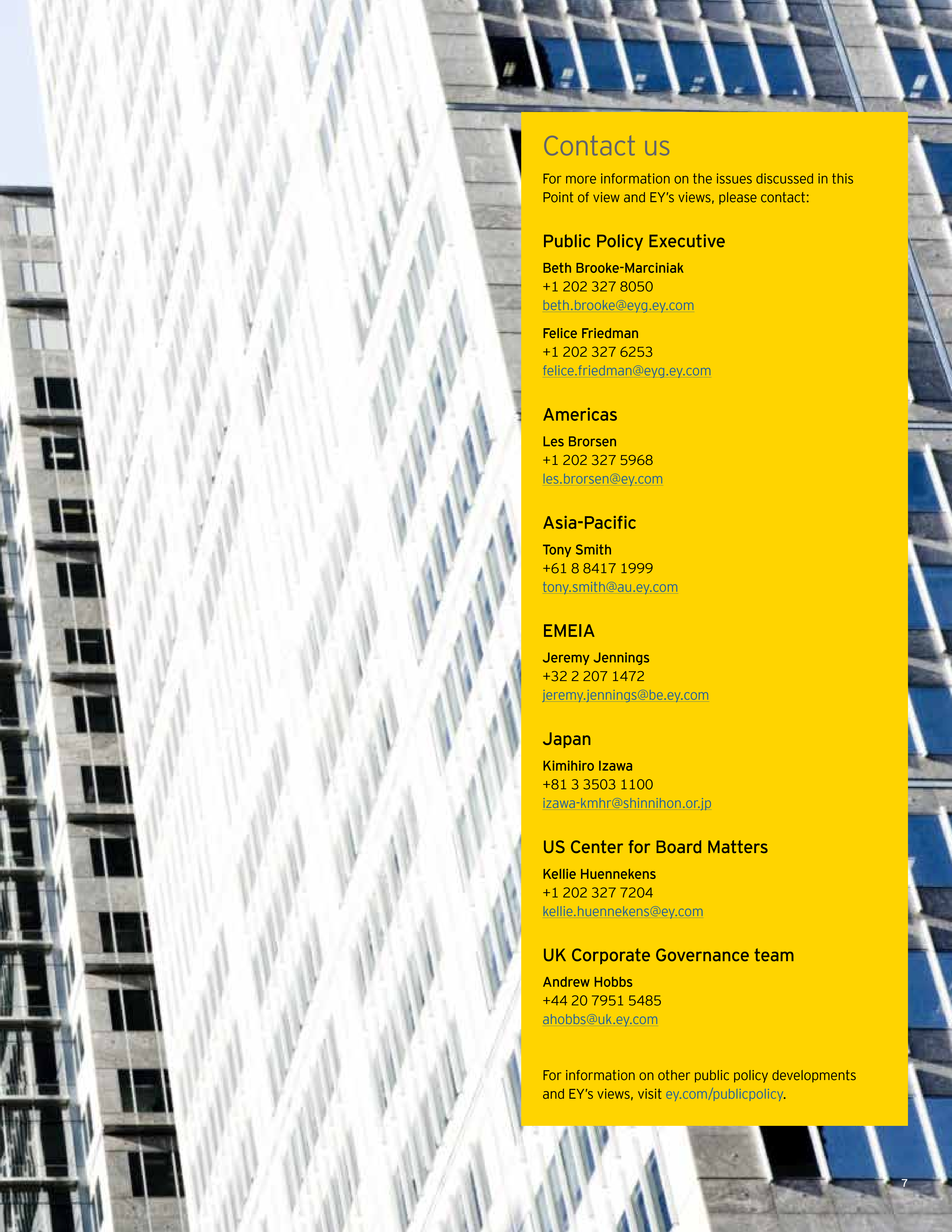
- A small number of companies provide a statement about industry expertise on the board, while many companies include information about industry expertise within the board director biographies.
- Many companies provide a statement about the board's approach to diversity. This is consistent with the focus on improving board diversity in many markets.

Conclusion

Our latest study highlights some modest increases in the number of audit committee-related disclosures since the 2014 reporting season. Nevertheless, our findings show there remains significant scope for audit committees to provide further insights of relevance to investors and others, including about how they carry out their important audit oversight role. This will help give investors and others the information they need to assess the effectiveness of audit committees and the external auditor.

Summary table

Disclosure topic	Average across five markets		Australia		Canada		Singapore		UK		USA	
	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2
Description of topics discussed by the audit committee	36%	36%	13%	15%	53%	58%	7%	0%	99%	99%	7%	8%
Explicit statement that the audit committee is responsible for the appointment, compensation and oversight of the auditor	54%	58%	40%	35%	55%	57%	50%	60%	57%	66%	66%	71%
Disclosure of the factors used in the audit committee's assessment of the auditor's qualifications and work quality	35%	37%	17%	17%	10%	20%	33%	47%	80%	62%	34%	39%
Statement that the audit committee considers non-audit fees/services when assessing auditor independence	80%	80%	94%	94%	37%	35%	97%	97%	94%	92%	80%	80%
Disclosure of length of auditor tenure	45%	48%	27%	29%	57%	62%	3%	3%	88%	85%	50%	59%
Statement that the audit committee is independent		75%		58%		87%		60%		70%		100%
Statement that at least one audit committee member has financial expertise		75%		40%		67%		77%		93%		100%
Discussion of diversity of audit committee members and any policy on diversity (specific to the audit committee and not the board as a whole)		0%		0%		2%		0%		0%		0%
Statement that at least one member of the audit committee has relevant industry expertise		11%		21%		10%		10%		15%		0%
Statement that the audit committee is responsible for fee negotiations		15%		6%		0%		10%		36%		21%
Explanation provided for changes in audit fees paid to external auditor		5%		0%		10%		0%		5%		9%
Disclosure of the year the lead audit partner was appointed		39%		31%		5%		93%		57%		9%
Statement that choice of external auditor is in the best interests of company and/or shareholders		13%		0%		0%		0%		8%		58%
Statement that the audit committee considers the impact of changing auditors when assessing whether to retain the current external auditor		15%		6%		3%		0%		23%		41%



Contact us

For more information on the issues discussed in this Point of view and EY's views, please contact:

Public Policy Executive

Beth Brooke-Marciniak
+1 202 327 8050
beth.brooke@eyg.ey.com

Felice Friedman
+1 202 327 6253
felice.friedman@eyg.ey.com

Americas

Les Brorsen
+1 202 327 5968
les.brorsen@ey.com

Asia-Pacific

Tony Smith
+61 8 8417 1999
tony.smith@au.ey.com

EMEIA

Jeremy Jennings
+32 2 207 1472
jeremy.jennings@be.ey.com

Japan

Kimihiro Izawa
+81 3 3503 1100
izawa-kmhr@shinnihon.or.jp

US Center for Board Matters

Kellie Huennekens
+1 202 327 7204
kellie.huennekens@ey.com

UK Corporate Governance team

Andrew Hobbs
+44 20 7951 5485
ahobbs@uk.ey.com

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