ENHANCING THE AUDIT COMMITTEE REPORT

A CALL TO ACTION

NACD
NATIONAL ASSOCIATION OF CORPORATE DIRECTORS

CORPORATE BOARD MEMBER
An NYSE Euronext Company

Tapestry Networks

THE DIRECTORS' COUNCIL

AACM Inc.

CENTER FOR AUDIT QUALITY
Serving Investors, Public Company Auditors & the Markets

AuditCommitteeCollaboration.org

PREFACE

In 2012, several nationally recognized U.S. governance organizations[1] came together to collaborate on projects intended to leverage their efforts to expand audit committee member access to useful tools and materials across the spectrum of public companies to strengthen audit committee performance and transparency. Known as the Audit Committee Collaboration, one of our first projects was the production of a tool for assisting audit committees with their annual assessment of the external auditor.[2]

An area of recent focus for us has been audit committee reporting. We believe that greater transparency about the audit committee's roles and responsibilities is one way of increasing investor confidence, and an opportunity to communicate more clearly to shareholders about audit committee-related activities. To this end, we believe that public company audit committee reporting can and should be strengthened, and we encourage all public company audit committees to renew their focus on this important issue.

1. This collaborative effort is known as the "Audit Committee Collaboration" and, for purposes of this particular initiative, consists of the following organizations: the National Association of Corporate Directors, Corporate Board Member/NYSE Euronext, Tapestry Networks, the Directors' Council, the Association of Audit Committee Members, Inc., and the Center for Audit Quality.

2. This tool, made available by the Audit Committee Collaboration in October 2012, provides audit committees with a practical, customizable resource that aids the audit committee in conducting its annual assessment of the external auditor. [http://www.thecaq.org/docs/reports-and-publications/annualauditorevaluationtoolinteractive.pdf?sfvrsn=2]

EXECUTIVE SUMMARY

We encourage all public company audit committees to thoughtfully reassess their reporting and communication with stakeholders and, if need be, to strengthen them in the future.

This "Call to Action" is based upon the simple premise that, given the importance of the audit committee's responsibilities for broadly overseeing the financial statement process, including the work of the external and internal auditors, it is important for investors and others with a stake in our financial markets to understand and have confidence in the audit committee's work. The annual audit committee report included in the proxy statement is the principal source of public audit committee-related information other than its committee charter. Public disclosures are the primary channel through which audit committees can educate investors and other stakeholders about their critical responsibilities, and demonstrate their effectiveness in executing those responsibilities. Thus, *we encourage all public company audit committees to thoughtfully reassess their reporting and communication with stakeholders and, if need be, to strengthen them in the future.*

We also recognize that additional forces are at work: there are certain external drivers of change, grounded in legislative and regulatory actions that have expanded the responsibilities of the audit committee in recent years. As the scope of audit committees' responsibilities has grown, so too have regulators' and investors' interest in the way in which they are carried out.

Importantly, we note a growing trend among a number of leading audit committees that are voluntarily addressing the need for enhanced audit committee reporting in order to strengthen confidence and communication. We give examples of their disclosure language, pulled directly from 2013 proxy statements, which demonstrate emerging practices in key areas. While not intending to be prescriptive or suggest a mandate, these leading disclosure examples provide benchmarks that other audit committees can use to evaluate how effectively their own disclosures:

- Clarify the scope of the audit committee's duties
- Clearly define the audit committee's composition
- Provide relevant information about:
  - Factors considered when selecting or reappointing an audit firm
  - Selection of the lead audit engagement partner
  - Factors considered when determining auditor compensation
  - How the committee oversees the external auditor
  - The evaluation of the external auditor

CALL TO ACTION

We call on 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.

Each public company is unique in size and complexity, and operates within a constantly changing and distinct set of circumstances. In addition to the multitude of factors differentiating companies, the scope of an audit committee's responsibilities also may vary from company to company. Thus, we do not believe a prescriptive approach to audit committee disclosure is appropriate or workable; indeed, such an approach is not compatible with the goal of providing more individualized and meaningful information. We believe each company's audit committee is in the best position to determine what improvements, if any, are needed to its communications for a particular reporting period.

We acknowledge and share the perennial concern about information overload,[3] and we commend efforts to identify duplicative requirements, simplify disclosure, and modernize reporting processes so investors have more effective and efficient access to the information they need for their investment and voting decisions. Such a holistic review and restructuring of the corporate disclosure framework will require participation by all relevant stakeholders (e.g., regulators, U.S. securities exchanges, those charged with governance and those with the responsibility to prepare and review disclosures) and is likely to take months, if not years, to complete.

In the meantime, we believe audit committees should critically evaluate their disclosures and carefully consider whether improvements can be made to provide investors with more relevant information that conveys that an informed, actively engaged and independent audit committee is carrying out its duties. If so, we encourage audit committees to begin taking the necessary steps with those charged with governance in their organizations to strengthen such disclosures accordingly.

We recognize that some disclosures about audit committee-related activities may appear outside the audit committee report, elsewhere in the proxy statement, in the annual report, or on a company's website. However, a complete understanding of the audit committee's activities would require a close analysis of the information in each of these different places. For investors, navigating and mining for information across disparate sources is likely suboptimal. We encourage audit committees and boards to take a fresh look at the format and, in some cases, the different channels that communicate audit committee-related activities and strive to streamline, link to, or consolidate where possible.

In performing a disclosure review, the audit committee should coordinate with its full board, offices of the corporate secretary and general counsel, and company management; it should also consider whether these and other resources within the company, including internal audit, might provide assistance. We believe a comprehensive and collaborative process will yield increased investor understanding of the important work audit committees are doing, as well as increased investor confidence in the public companies upon whose boards of directors they serve.

3. Similar concerns about information overload have been expressed by Mary Jo White, Chair of the U.S. Securities and Exchange Commission, October 15, 2013, at the National Association of Corporate Directors - Leadership Conference 2013. Her remarks, "The Path Forward on Disclosure" can be found here: [http://www.sec.gov/News/Speech/Detail/Speech/1370539878806#.UoJQ8ego6rR]

DRIVERS OF CHANGE

Regulator's and Standard Setter's Interest in the Audit Committee

Over ten years ago, the roles and responsibilities of audit committees of public companies were heightened in the United States with the passage of the Sarbanes-Oxley Act of 2002 (SOX). Among a number of requirements aimed at enhancing the independence of the external auditor of public companies, SOX explicitly mandated that the independent audit committee, not management, be directly responsible for appointing, compensating, and overseeing the external auditor. Adoption of this provision essentially codified recommendation number six of the 1999 report of the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees, co-chaired by Ira Millstein and John Whitehead,[4] and followed previous actions by the U.S. Securities and Exchange Commission (SEC), U.S. securities exchanges, and others to codify many other recommendations in that seminal report. SOX further stipulated that the audit committee is to be afforded the funding it determines appropriate for compensating the auditor and any advisers it may employ.

In the wake of the worldwide economic crisis, and as evidenced by various work plans, reports and proposals, regulators and standard setters across the globe have placed a renewed emphasis on the roles and contributions of audit committees and auditors towards the maintenance of financial stability and investor confidence. This is particularly noticeable in that regulators are assessing how audit committees fulfill their primary role to assist the board of directors with the oversight over a financial reporting system that is accountable to and meets the needs of investors.

From the U.S. Public Company Accounting Oversight Board (PCAOB):

> *In connection with its 2012-2016 Strategic Plan, the PCAOB identified as a near-term priority a project to "enhanc[e] PCAOB's outreach to and interaction with audit committees to constructively engage in areas of common interest, including auditor independence and audit quality."*[5] *The PCAOB expanded on this strategic priority in 2013 by noting the Board's outreach efforts with audit committees would be aimed at, among others, "enhancing the ability of audit committees to evaluate the independence, objectivity and skepticism of their auditors…[and] in finding ways for the PCAOB and audit committees to collaborate on efforts to enhance communication and interaction with investors about matters of interest to them, consistent with the respective roles and responsibilities of the Board and audit committees."*[6]

4. Report and Recommendations of the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees, published by the New York Stock Exchange and National Association of Securities Dealers, 1999. [http://www.chugachelectric.com/pdfs/agenda/fcagenda_051403_ixd.pdf]

5. PCAOB Strategic Plan: "Improving the Relevance and Quality of the Audit for the Protection and Benefit of Investors," November 30, 2012, p.5. [http://pcaobus.org/About/Ops/Documents/Strategic%20Plans/2012-2016.pdf]

6. PCAOB Standing Advisory Group Meeting: Audit Committee Outreach, May 15-16, 2013, p 2. [http://pcaobus.org/News/Events/Documents/05152013_SAGMeeting/Audit_Committee_Outreach.pdf]

From the Canadian Public Accountability Board (CPAB):

> *CPAB believes that audit committees can – and should – be key contributors to audit quality. Effective audit committees and auditors build confidence in the integrity of financial reporting. By doing so, they reduce financing costs and contribute to an efficient allocation of capital to fuel economic growth.*[7]

From the International Auditing and Assurance Standards Board (IAASB):

> *While users are likely to conclude that the active involvement of a high-quality audit committee will have a positive impact on audit quality, there is considerable variability in the degree to which audit committees communicate to users the way they have fulfilled these responsibilities. There is potential for fuller disclosure of the activities of audit committees to benefit both actual audit quality and user perception of it. Consequently, some countries are actively exploring whether to include more information in annual reports about the activities of audit committees in relation to the external audit.*[8]

Investor Interest in the Audit Committee

Investors, too, are increasing their focus on the activities and transparency of audit committees, particularly as those activities relate to enhanced audit quality through oversight of the independent external auditor. For example, on April 19, 2013, the Council for Institutional Investors (CII) approved an expansion of its Policies on Corporate Governance to identify how audit committees can use their authority to promote auditor independence and audit quality. The revised section (2.13a) reads, in part, *"The audit committee report should provide meaningful information to investors about how the committee carries out its responsibilities. The report should include an explanation of how the committee carries out its auditor compensation responsibilities in consideration of audit quality objectives."*[9]

Some investors are also seeking greater disclosure from audit committees of a number of companies around matters such as the responsibility of the audit committee for the appointment, compensation and oversight of the external auditor, audit firm tenure, audit firm fee determinations, and audit committee involvement in the selection of the audit engagement partner.[10]

On a broader, more global scale, investors and observers identified "the role of audit committees and communication between regulators and audit committees" as an area for attention by the International Forum of Independent Audit Regulators (IFIAR) in its plenary meetings or in working groups, and this issue is a key element of IFIAR's most recent work plan.[11]

7. CPAB Report "Effective Regulation – Sustainable Solutions: Report on the 2012 Inspections of the Quality of Audits Conducted by Public Accounting Firms," April 4, 2013, p. 9. [http://www.cpab-ccrc.ca/EN/content/CPAB_Public_Report_2012_Eng.pdf]

8. IAASB, "A Framework for Audit Quality," January 15, 2013, p. 48. [http://www.ifac.org/publications-resources/framework-audit-quality]

9. CII, Policies on Corporate Governance, Section 2.13a, April 19, 2013. [http://www.cii.org/corp_gov_policies]

10. In the 2012 and 2013 proxy seasons, the pension fund of the United Brotherhood of Carpenters wrote letters to a number of companies seeking additional audit committee disclosures related to their responsibilities with regard to the external auditor. Additionally, at a March 2013 meeting of members of the Audit Committee Leadership Networks in North America and Europe, Blackrock Inc. managing director and global head of corporate governance, Michelle Edkins, noted that the audit committee's process for overseeing the external audit and auditor was among several elements that investors would be interested in seeing in the audit committee report. Tapestry Networks, ViewPoints, Issue 21, May 2, 2013, p. 7. [http://www.tapestrynetworks.com/initiatives/corporate-governance/global-audit-committee-leadership-networks/upload/Tapestry_EY_ACLS_Summit_View21-May13.pdf]

11. IFIAR Officers' Work Plan for Term April 2013-April 2015, Section 3 – Thought Leadership, p. 4. [https://www.ifiar.org/IFIAR/media/Images/High-Level-Summary-of-the-2013-2015-IFIAR-Officers-Work-Plan.pdf]

Strengthening Confidence and Communication through Audit Committee Reporting

Audit committee members are taking note of the increased interest in their roles and responsibilities by regulators, investors and others. In its Summary of Proceedings from a June 19, 2013 meeting of the Audit Committee Chair Advisory Council, the National Association of Corporate Directors (NACD) reports that "[s]everal delegates acknowledged that many audit committees' disclosures are fairly minimalistic: *'Frankly, we don't do a good job of communicating what we do. The public doesn't see all the work we do, quarter after quarter.'*" [12]

And at a March 2013 Tapestry Networks' summit of audit committee chairs across North America and Europe, participants focused on the issue of enhanced audit committee reporting. One of the themes that emerged was the recognition that *"[r]egulators, policy-makers, and many investors would benefit from a more robust understanding of what the public company audit committee does and how it oversees the external audit firm and performs its other responsibilities."* [13]

Importantly, studies of recent public disclosures (found in both audit committee reports and elsewhere in the proxy statement) show that a number of audit committees are already embracing disclosures that go beyond the minimum requirements of the SEC and U.S. exchanges. Proxy statement reviews by Ernst & Young's (EY) Corporate Governance Center and Deloitte LLP reveal strengthened disclosures in a range of areas: their processes for conducting periodic evaluations of their independent auditors, their rationales for recommending the retention or replacement of their external auditors, how they carry out their responsibilities for compensating their auditors, how they promote auditor independence and skepticism, the tenures of the auditors, the types of information they discuss with their auditors, and their roles in selecting the lead audit engagement partner.

12. NACD Summary of Proceedings, Audit Committee Chair Advisory Council, June 19, 2013, p. 6. [http://nacd.files.cms-plus.com/FileDownloads/PDF/NACD%20Audit%20Committee%20Chair%20Advisory%20Council%20SOP%20-%20June%2019%202013.pdf]

13. Tapestry Networks, ViewPoints, Issue 22, May 2, 2013, p.1. [http://www.tapestrynetworks.com/initiatives/corporate-governance/global-audit-committee-leadership-networks/upload/Tapestry_EY_ACLS_Summit_View22-May13.pdf]

EMERGING PRACTICES

The table below illustrates data from the most recent EY proxy statement review of the Fortune 100 to highlight the percentage of companies whose audit committee disclosures go beyond minimum regulatory and securities exchange requirements in certain areas. (Examples of 2013 disclosure language can be found beginning on page 9 of this report.)

Observable Audit Committee Disclosures Beyond Minimum Requirements	Percentage of Companies that Disclosed Pursuant to the EY Report [14]
Affirmative statement that the audit committee is responsible for the appointment, compensation and oversight of the external auditor	50%
Disclosure of the length of the external auditor's tenure	31%
The audit committee was involved in the selection of the lead audit partner	17%

Informative disclosures around topics such as those depicted in the table, can increase the trust and confidence of investors, as they demonstrate that audit committees understand and represent a range of investor interests while discharging with due care their oversight responsibilities over the financial reporting process and the external auditor. As such, these emerging and voluntary disclosure practices are important markers in the continuing evolution of the corporate governance and disclosure system that underpins the U.S. capital markets.

The following are sample areas in which audit committees should consider improving their related disclosures, with illustrations of emerging practices for each area.[15]

Clarify the scope of the audit committee's duties. All audit committees of companies listed on the New York Stock Exchange (NYSE) and NASDAQ must include their specific duties in their charters.[16] NYSE listing rules require that public company audit committee charters be located on the company's website,[17] and that its listed companies also provide a link to the charter somewhere in their proxy

14. EY "Audit Committee Reporting to Shareholders – 2013 Proxy Season Update," September 2013. This disclosure is part of the EY report that updates an EY February 2013 analysis that reviewed the 2012 audit committee-related disclosures of the Fortune 100 companies to determine whether companies already provide information over and above what is required under current disclosure laws and rules. [http://www.ey.com/Publication/vwLUAssets/Audit_committee_reporting_2013_proxy_season_update/$FILE/Audit_committee_reporting_shareholder_2013_proxy_season_update.pdf]

15. In making a reference in this document to a specific company or its audit committee's disclosures, the Audit Committee Collaboration is not opining on the legal merits of the disclosures. Additionally, reference to a specific company's disclosures should not be construed to mean that the company endorses this document or consider their disclosures a "call to action" to any other company or audit committee.

16. Refer to NYSE Rule 303A.07 [http://nysemanual.nyse.com/lcm/Help/mapContent.asp?sec=lcm-sections&title=sx-ruling-nyse-policymanual_303A.05&id=chp_1_4_3_8] and NASDAQ Rule 5605(c)(1). [http://nasdaq.cchwallstreet.com/NASDAQTools/PlatformViewer.asp?selectednode=chp%5F1%5F1%5F4%5F4&manual=%2Fnasdaq%2Fmain%2Fnasdaq%2Dequityrules%2F]

17. Refer to NYSE requirement in 303A.07(b)(ii). [http://nysemanual.nyse.com/lcm/Help/mapContent.asp?sec=lcm-sections&title=sx-ruling-nyse-policymanual_303A.05&id=chp_1_4_3_8]

statements.[18] Given the importance of increasing the public's understanding of the role of the audit committee, the audit committee should ensure that its charter is easy to locate, and might consider providing at a minimum the link and, where relevant, more disclosure in the audit committee report around key provisions of the charter, such as its responsibilities regarding the external auditor. While disclosures related to the audit committee's responsibilities with regard to the independent auditor are important given the statutory mandate for these duties, disclosures regarding risk oversight have become an important topic of discussion.[19] To the extent that an audit committee has responsibility for the oversight of risk other than financial reporting, this may be an area to explore.[20]

...Under its charter, the Audit Committee is responsible for overseeing our accounting and financial reporting processes and audits of our financial statements. The Audit Committee is directly responsible for the appointment and oversight of our independent auditors, including review of their qualifications, independence and performance.

Among other duties, the Audit Committee also oversees:

- the integrity of our financial statements, our accounting and financial reporting processes, our systems of internal control over financial reporting and safeguarding our assets;
- our compliance with legal and regulatory requirements;
- the performance of our internal auditors and internal audit functions; and
- our guidelines and policies with respect to risk assessment and risk management.

The Audit Committee has established procedures for the receipt, retention and treatment, on a confidential basis, of any complaints we receive. We encourage employees and third-party individuals and organizations to report concerns about our accounting controls, auditing matters or anything else that appears to involve financial or other wrongdoing. To report such matters, please e-mail us at: mdlz-financialintegrity@mdlz.com...

Source: Mondelēz International 2013 Definitive Proxy Statement

18. Refer to NYSE requirement in 303A.07(b)(iii). [http://nysemanual.nyse.com/lcm/Help/mapContent.asp?sec=lcm-sections&title=sx-ruling-nyse-policymanual_303A.05&id=chp_1_4_3_8]

19. The Federation of European Accountants, the Institute of Chartered Accountants (Australia) and the Center for Audit Quality co-sponsored three roundtable discussions in Brussels, Hong Kong, and New York City offering a forum for representatives from the global audit committee community to share views on the current state of audit committee performance, including leading practices. Notably, there was a focus at all three roundtables on disclosures related to oversight of risk management. There was a shared belief across all jurisdictions that the potential overlap in the membership between the audit committee and risk committee (if one exists) is important to fostering effective communication on key issues related to risk oversight. The findings can be found in "Global Observations on the Role of the Audit Committee – A Summary of Roundtable Discussions." [http://www.thecaq.org/docs/reports-and-publications/globalobservationsontheroleoftheauditcommittee.pdf?sfvrsn=2]

20. While ultimate responsibility for oversight of risk management lies with the full board, some boards have asked their audit committees to oversee certain areas of risk management, or have impaneled dedicated risk oversight committees. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Federal Reserve was given the task of issuing new rules requiring certain large banks to establish a board risk committee with a formal written charter approved by the company's board of directors.

More effective disclosure by an audit committee about its specific duties, including those that are mandated with respect to the independent auditor, can inform investors about the audit committee's important role in maintaining the highest standards of audit quality and financial reporting. The audit committee might consider, for example, whether it is important to disclose more information about its responsibility under SOX for establishing procedures for the anonymous receipt, retention, and treatment of issuer or employee complaints regarding accounting or auditing matters.

...Throughout the year, the Audit Committee was involved in monitoring the Ethicspoint® reporting system which was acquired and implemented in 2003 to assist the Audit Committee in administering the anonymous complaint procedures outlined in the Code of Business Conduct and Ethics. The Sarbanes-Oxley Act of 2002 required that the Audit Committee establish procedures for the confidential submission of employee concerns regarding questionable accounting, internal controls or auditing matters. The Audit Committee will continue to ensure that the Company is in compliance with all applicable rules and regulations with respect to the submission to the Audit Committee of anonymous complaints from employees of the Company...

Source: Old National Bancorp 2013 Definitive Proxy Statement

Clearly define the audit committee's composition. In the context of regulator and securities exchange requirements, disclosures associated with the reporting of audit committee qualifications and independence can vary. The audit committee should consider providing more clarity around such elements as its members' qualifications and independence, and the basis upon which these qualities are determined.

...The Audit Committee is composed of six non-employee directors and operates under a written charter adopted by the Board of Directors that was last amended on April 23, 2013. The Board of Directors has determined that each member of the Audit Committee is "independent" and financially literate, and that at least one member has accounting or other related financial management expertise, in each case as such qualifications are defined under the Listing Standards of the New York Stock Exchange. The Board of Directors has also determined that each of [Member A] and [Members B, C, and D] qualifies as an "audit committee financial expert" as defined by the SEC...

Source: Legg Mason, Inc. 2013 Definitive Proxy Statement

Disclose relevant factors the audit committee considers when selecting or reappointing an audit firm. The audit committee should consider providing more effective disclosure about the factors it considers when making its determination about engaging an audit firm. In the context of appointing or reappointing the independent audit firm, the audit committee should consider discussing the quality and qualifications of the firm, and might include things such as capacity to staff the audit, geographical reach of the practice, and industry or sector specific expertise. In addition, the audit committee should consider providing relevant information from its annual evaluation of the external auditor,[21] as well as other information it believed was critical to its appointment or reappointment considerations. Providing context around the decision to appoint or reappoint an audit firm can help build investor confidence by underscoring the thoroughness of the process that led to the audit committee's decision. EY found that 21 percent (up from 18 percent the previous year) of reviewed companies disclose factors the audit committee considers in its process for the evaluation of the quality and qualifications of the external audit firm.[22]

...In determining whether to reappoint [Independent Auditor] as Prudential Financial's independent auditor, the Audit Committee took into consideration a number of factors, including the length of time the firm has been engaged, the quality of the Audit Committee's ongoing discussions with [Independent Auditor] and an assessment of the professional qualifications and past performance of the Lead Audit Partner and [Independent Auditor]...

Source: Prudential Financial, Inc. 2013 Definitive Proxy Statement

...The Audit Committee annually reviews [Independent Auditor's] independence and performance in connection with the committee's determination of whether to retain [Independent Auditor] or engage another firm as our independent auditor. In the course of these reviews, the committee considers, among other things:

- [Independent Auditor's] historical and recent performance on the GE audit, including the results of an internal survey of [Independent Auditor's] service and quality;
- an analysis of [Independent Auditor's] known legal risks and significant proceedings;
- external data relating to audit quality and performance, including recent Public Company Accounting Oversight Board (PCAOB) reports on [Independent Auditor] and its peer firms;
- the appropriateness of [Independent Auditor's] fees, on both an absolute basis and as compared to its peer firms;
- [Independent Auditor's] tenure as our independent auditor and its familiarity with our global operations and businesses, accounting policies and practices and internal control over financial reporting;
- [Independent Auditor's] capability and expertise in handling the breadth and complexity of our worldwide operations; and
- [Independent Auditor's] independence.

Based on this evaluation, the Audit Committee believes that [Independent Auditor] is independent and that it is in the best interests of GE and our shareowners to retain [Independent Auditor] to serve as our independent auditor for 2013...

Source: General Electric Company 2013 Definitive Proxy Statement

21. The Collaborative partners joined forces in October 2012 to launch a new tool to assist audit committees in performing an annual evaluation of the external auditor in order to make an informed recommendation to the Board whether to retain the auditor. [http://www.thecaq.org/docs/reports-and-publications/annualauditorevaluationtoolinteractive.pdf?sfvrsn=2]

22. EY "Audit Committee Reporting to Shareholders – 2013 Proxy Season Update," September 2013.

Provide relevant information about the audit committee's involvement in the selection of the lead audit engagement partner. Another important provision of SOX designed to support auditor independence is the mandatory rotation of the lead audit partner after five years. The audit committee should consider more effective disclosure about its process and involvement in the selection of a new lead audit engagement partner. EY found that 17 percent (up from 1 percent in its previous review) of audit committee reports reviewed included a statement that the audit committee is involved in the selection of the lead partner.[23]

...In accordance with SEC rules and [Independent Auditor's] policies, audit partners are subject to rotation requirements to limit the number of consecutive years an individual partner may provide service to our Company. For lead and concurring audit partners, the maximum number of consecutive years of service in that capacity is five years. The process for selection of the Company's lead audit partner pursuant to this rotation policy involves a meeting between the Chair of the Audit Committee and the candidate for the role, as well as discussion by the full Committee and with management...

Source: Pfizer Inc. 2013 Definitive Proxy Statement

Provide relevant factors the audit committee considers when determining auditor compensation. The role the audit committee plays (rather than management) in determining appropriate compensation of the external auditor provides the ability to promote auditor independence. Disclosure of key factors the audit committee considered in this process could help investors understand the direct and primary role the audit committee played, and the important balance the audit committee struck in ensuring that the auditor is paid a reasonable amount that is consistent with the delivery of a quality audit. Linking this type of contextual information to compensation policies or decisions could be useful to those seeking to better understand the appropriateness of audit firm compensation.

...Audit Fees represent fees for professional services provided in connection with the audit of our consolidated annual financial statements and internal control over financial reporting and reviews of our quarterly financial statements, as well as audits of subsidiary financial statements (including statutory audits), regulatory filings, consents and other SEC matters. Audit Fees increased in 2012 primarily due to the audit of the standalone financial statements of our subsidiary, Blackhawk Network Holdings, Inc....

Source: Safeway Inc. 2013 Definitive Proxy Statement

23. Ibid.

SEC rules require public companies to disclose in the proxy the total compensation paid to the external auditor – both related to the audit as well as for non-audit services. Because of its responsibility for preapproval of such services, the audit committee should consider greater transparency around this activity. Many public companies are already doing so; Deloitte LLP found that 29 percent of the audit committee reports it reviewed contained enhanced disclosure of the audit committee's approval and preapproval of audit and non-audit services.[24] Further, EY found that 79 percent of companies in its review disclose that the audit committee considers the effect of compensation for non-audit services on the external auditor's independence, either in the audit committee report or elsewhere in the proxy statement.[25]

… The Committee has reviewed and approved the amount of fees paid to the independent auditors for audit, audit related and tax compliance services. The Committee concluded that the provision of services by the independent auditors is compatible with the maintenance of their independence. [Independent Auditor] has served as the independent registered public accounting firm of Citi and its predecessors since 1969. As in prior years, Citi and its Committee have engaged in a review of [Independent Auditor] in connection with the Committee's consideration of whether to recommend that shareholders ratify the selection of [Independent Auditor] as Citi's independent auditor for the following year. In that review, the Committee considers both the continued independence of [Independent Auditor] and whether retaining [Independent Auditor] is in the best interests of Citi and its stockholders. Citi's management prepares an annual assessment of [Independent Auditor] for the Audit Committee that includes (i) the results of a management survey of [Independent Auditor's] overall performance, (ii) an analysis of [Independent Auditor's] known legal risks and significant proceedings that may impair [Independent Auditor] ability to perform Citi's annual audit; and (iii) [Independent Auditor's] fees and services provided to Citi both on an absolute basis, noting, of course, that [Independent Auditor] does not provide any non-audit services, other than those described in the Proxy Statement, to Citi, and compared to services provided by other auditing firms to peer institutions.

Source: Citigroup Inc. 2013 Definitive Proxy Statement

24. Deloitte's 2013 analysis of S&P 100 companies that filed their proxy statements March 1, 2013 through May 31, 2013. The focus of the analysis was to assess current requirements with respect to audit committee reports and to highlight areas where many audit committees are going beyond the required elements and providing additional transparency into their practices. NOTE: As of the date of the issuance of this report, the Deloitte analysis had not been publicly released. It is expected to be released late in 2013 and will be available at http://www.corpgov.deloitte.com/site/us/.

25. EY "Audit Committee Reporting to Shareholders – 2013 Proxy Season Update," September 2013.

Provide relevant information about how the audit committee oversees the external auditor. The audit committee should also consider whether additional disclosure about its general oversight of the external auditor – either through descriptions of processes or specific activities – would provide shareholders and potential investors with useful context. These might include discussions of the degree of the audit committee's interaction with the external auditor (including the nature or number of meetings outside the presence of management), the types of issues discussed at those meetings, and other activities that are central to the audit committee's oversight.

...The Committee is responsible for the engagement of the independent auditor and appointed [Independent Auditor] to serve in that capacity during 2012 and 2013. In that connection, the Committee:

- reviewed [Independent Auditor's] independence from the Company and management, including [Independent Auditor's] written disclosures described above;
- reviewed periodically the level of fees approved for payment to [Independent Auditor] and the pre-approved non-audit services it has provided to the Company to ensure their compatibility with [Independent Auditor's] independence; and
- reviewed [Independent Auditor's] performance, qualifications and quality control procedures.

Among other matters, the Committee also:

- reviewed the scope of and overall plans for the annual audit and the internal audit program;
- consulted with management and [Independent Auditor] with respect to the Company's processes for risk assessment and risk management;
- reviewed and approved the Company's policy with regard to the hiring of former employees of the independent auditor;
- reviewed and approved the Company's policy for the pre-approval of audit and permitted non-audit services by the independent auditor;
- received reports pursuant to the Company's policy for the submission and confidential treatment of communications from employees and others about accounting, internal controls and auditing matters;
- reviewed with management the scope and effectiveness of the Company's disclosure controls and procedures, including for purposes of evaluating the accuracy and fair presentation of the Company's financial statements in connection with certifications made by the CEO and CFO;
- reviewed significant legal developments and the Company's processes for monitoring compliance with law and Company policies; and
- reviewed the Company's related person transactions.

Source: McDonald's Corporation 2013 Definitive Proxy Statement

The SEC requires the audit committee to state in its report that the external auditor has discussed with the audit committee the required communication matters under applicable standards, such as those in PCAOB Auditing Standard No. 16 (AS 16).[26] Under AS 16, the auditor is required to communicate the overall audit strategy, difficult or contentious matters for which the auditor consulted outside the engagement team, information about the nature and extent of specialized skills needed and the extent of planned use of internal auditors or other third parties. Disclosing that significant or relevant topic areas were addressed in conversations with the auditor could provide market participants with a greater understanding of the company.[27] EY found that 8 percent (up from 6 percent in its previous review) of companies reviewed disclosed topics discussed by the audit committee and the external auditor (beyond what is required).[28]

…Prior to their issuance, we reviewed and discussed the quarterly and annual earnings press releases, consolidated financial statements (including the presentation of non-GAAP financial information) and disclosures under "Management's Discussion and Analysis of Financial Condition and Results of Operations" (including significant accounting policies and judgments) with management, Comcast's internal auditors and the independent auditors. We also reviewed Comcast's policies and practices with respect to financial risk assessment, as well as its processes and practices with respect to enterprise risk assessment and management. We discussed with the independent auditors matters required to be discussed by Statement on Auditing Standards No. 61 (Communication with Audit Committees), as amended, and Rule 2-07 (Communication with Audit Committees) of Regulation S-X.

We discussed with the independent auditors the overall scope and plans for their audit and approved the terms of their engagement letter. We also reviewed Comcast's internal audit plan. We met with the independent auditors and with Comcast's internal auditors, in each case, with and without other members of management present, to discuss the results of their respective examinations, the evaluations of Comcast's internal controls and the overall quality and integrity of Comcast's financial reporting…

Source: Comcast Corporation 2013 Definitive Proxy Statement

26. Refer to SEC Regulation S-X §210.2-07, Communication with audit committees.
27. PCAOB and IAASB currently have proposals pending that would impact reporting by the auditor about critical or key audit matters.
28. EY "Audit Committee Reporting to Shareholders – 2013 Proxy Season Update," September 2013.

Provide relevant information about how the audit committee evaluates the external auditor. Most audit committees have practices in place to assess the effectiveness of their auditor throughout the year. The audit committee should consider providing information about its evaluation process, or providing key conclusions from that evaluation with regard to any discussion about auditor reappointment.

…In its meetings with representatives of the Independent Auditors, the Audit Committee asks them to address, and discusses their responses to, several questions that the Audit Committee believes are particularly relevant to its oversight. These questions include:

Are there any significant accounting judgments or estimates made by management in preparing the financial statements that would have been made differently had the Independent Auditors themselves prepared and been responsible for the financial statements?

Based on the Independent Auditors' experience and their knowledge of the Company, do the Company's financial statements fairly present to investors, with clarity and completeness, the Company's financial position and performance for the reporting period in accordance with generally accepted accounting principles and SEC disclosure requirements?

Based on the Independent Auditors' experience and their knowledge of the Company, has the Company implemented internal controls and internal audit procedures that are appropriate for the Company?
The Audit Committee believes that, by thus focusing its discussions with the Independent Auditors, it can promote a meaningful dialogue that provides a basis for its oversight judgments…

Source: The Coca-Cola Company 2013 Definitive Proxy Statement

CONCLUSION

The effective communication of high-quality information among the key players in our financial markets promotes investor confidence – the engine that drives capital formation and the efficiency of markets. Therefore, we strongly encourage audit committees to respond to this Call to Action by exploring ways to continually improve the information they provide to the marketplace.

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Tapestry Networks

The Directors' Council

Association of Audit Committee Members, Inc.

The Center for Audit Quality

APPENDIX

The following is a short list of companies and links to their proxy statements which may contain additional useful examples of enhanced audit committee disclosures related to some of the areas discussed or referenced in this Call to Action. Some of these proxy statements were the source of examples in the body of this document.[29]

As discussed above, the disclosures of one company may not be appropriate for another public company. Because of the variability in company characteristics and circumstances, one size disclosure does not fit all, and the degree of comparability with other companies' disclosure is likely not the most appropriate standard by which to judge the quality of disclosure. There are thousands of public companies of various types, sizes and industry sectors. Audit committee disclosure and any enhancement thereof should be tailored to the unique facts and circumstances of each issuer.

- Apple Inc.
- Bank of America Corporation
- Caterpillar Inc.
- Citigroup Inc.
- The Coca-Cola Company
- Comcast Corporation
- General Electric Company
- Hess Corporation
- Legg Mason, Inc.
- Lockheed Martin Corporation
- McDonald's Corporation
- Mondelēz International
- Morgan Stanley
- Old National Bancorp
- PPG Industries, Inc.
- Pfizer Inc.
- Prudential Financial, Inc.
- Republic Bancorp, Inc.
- Safeway Inc.
- The TJX Companies, Inc.

29. In making a reference in this document to specific company or its audit committee disclosures, the Audit Committee Collaboration is not opining on the legal merits of the disclosures. Additionally, reference to a specific company's disclosures should not be construed to mean that the companies endorse this document or consider their disclosures a "call to action" to any other company or audit committee.

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