

How Does Your Audit Committee Disclosure Compare?

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Deloitte and EY both recently published studies about audit committee disclosure in the proxy statements of the largest companies. Deloitte examined the S&P 100 while EY concentrated on the Fortune 100. This time of post-season review for most companies provides an opportunity to benchmark and consider additional audit committee disclosures for next year.

Disclosure about the audit committee. Audit committees are increasingly providing information about their composition and responsibilities. The vast majority of large companies have more than one audit committee financial expert, with 86% at S&P 100 companies and 83% at Fortune 100 companies (35% name two experts and 48% have three or more). Audit committees of Fortune 100 companies generally meet nine times a year with four members whose average board tenure is eight years and average age is 63.

Ninety-one percent of S&P 100 companies included the committee's role in overseeing the financial reporting process. Thirty-two percent also indicated that their committees reviewed earnings releases with management and the auditor prior to their release, while 25% stated that the committee discussed the financial statements in advance of earnings announcements.

More than a majority of the S&P 100, 57%, disclosed that the committee reviews significant accounting policies, and 34% discuss the review of management judgments and/or accounting judgments. While nearly all of the S&P 100 companies disclosed the committee's role in overseeing risk, 37% specifically included cybersecurity risk.

Disclosure about the auditor. Audit committees are increasingly making an explicit statement regarding their responsibilities for the appointment, compensation and oversight of the independent auditor, with 87% of Fortune 100 companies. However, only 32% of those companies state that the committee is responsible for fee negotiations. Explanations about changes in audit fees tend to occur more often when fees increase. Similarly, only 20% of the S&P 100 companies disclose that the committee is responsible for audit fees, while 63% provide more general information about the committee's role in reviewing and approving fees.

In terms of interactions with the auditors, 65% of S&P 100 companies disclose separate meetings between the committees and the auditors, and 60% of those companies state that they discuss the scope of the audit plan with the auditors.

Sixty-one percent of S&P 100 audit committees talk about evaluating the independent auditor, with some companies describing factors in their decisions that involve analyses of auditor quality and performance, including the results of PCAOB and peer reviews, the auditors' knowledge and experience with the company and the industry and the appropriateness of the fees.

Seventy-five percent of the Fortune 100 companies, and 73% of the S&P 100 companies, disclose that the audit committee is involved in the selection of the lead engagement partner. For the Fortune 100 companies, 64% explicitly stated that the auditor is independent, and 84% of those companies indicate that the committee considers non-audit fees and services when assessing independence.

The recent PCAOB rules, which have not yet been approved by the SEC, would require companies to disclose the auditor's tenure. Of the Fortune 100 companies, 67% already provide this information and 60% of those companies state that the committee considers the impact of changing auditors when assessing whether to retain the current auditor.

Seventy-one percent of the S&P 100 companies disclose the auditor's tenure, highlighting the benefits of a long relationship that include allowing auditors to have a deeper understanding of companies' businesses, accounting policies and practices and internal control over financial reporting, which can also lead to more efficient fee structures and avoid significant costs and disruptions that would be associated with bringing in new auditors.

Another matter that the new PCAOB rules may affect is disclosure of the audit committee's discussions with the auditor. Only a very small number of companies currently provide such information, but that could change once auditors are required to report on critical audit matters.

Disclosure about internal audit. Eighty-nine percent of S&P 100 companies stated that the audit committee oversee the internal audit function, including the qualification and performance of the function and the internal auditors, meeting with them to discuss the scope and results of the internal audit plan and overseeing the appointment, review and compensation of the chief audit executives.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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