



September 1, 2015

Secretary  
Securities and Exchange Commission  
100 F Street NW  
Washington, DC 20549-1000

Re: File No. S7-13-15, *Possible Revisions to Audit Committee Disclosures*

Dear Secretary:

The Financial Reporting Committee (FRC) of the Institute of Management Accountants (IMA) is writing to share its views on the SEC's Concept Release File No. S7-13-15, *Possible Revisions to Audit Committee Disclosures* (Release). The IMA is a global association representing over 75,000 accountants and finance team professionals. Our members work inside organizations of various sizes, industries and types, including manufacturing and services, public and private enterprises, not-for-profit organizations, academic institutions, government entities and multinational corporations.

The FRC is the financial reporting technical committee of the IMA. The committee includes preparers of financial statements for some of the largest companies in the world, representatives from the world's largest accounting firms, valuation experts, accounting consultants, academics, and users. The FRC reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations. Additional information on the IMA and the committee can be found at [www.imanet.org](http://www.imanet.org) and in the Advocacy Activity section under the About IMA tab.

### **Overview**

Members of FRC interact with audit committees in various capacities and recognize the important role that those committees play in seeing that registrants are appropriately governed. Audit committees' oversight of financial reporting and internal controls in general, and specifically the controls over financial reporting, is an important contributor to efficient capital markets. We also believe that many shareholders and other users of corporate reports are not fully aware of audit committees' activities and for that reason we support improvement of audit committee disclosures. Voluntary efforts to improve those reports in annual meeting proxy statements led by the National Association of Corporate Directors, the Center for Audit Quality, and others in recent years have resulted in changes for the better but more can be done. Thus, we encourage this effort by the SEC and believe it can lead to improved communications between audit committees and investors.

We are, however, concerned about the general approach taken in the Release. First, the Release includes a long list of detailed questions, which could lead to consideration of all of those matters, ultimately resulting in very detailed rule proposals. Second, the Release focuses on the oversight of the external audit function even though that responsibility represents a minority of the audit committee's time and attention in most cases. This overemphasis could result in more SEC rules about the oversight of the external audit function with an implicit de-emphasis on equally important audit committee activities. These concerns lead us to provide an overview of the approach that we believe the SEC should take, instead of responding to the 74 detailed questions in the Release.



### **Provide Audit Committee Disclosures in a Single Location**

To be most useful, we believe audit committee disclosures should be provided in a single location so that investors can get complete information about the nature of the committee and its activities without having to search through several different SEC filings, other documents, etc. We believe that the best location for such a single, comprehensive report is the annual meeting proxy statement. That document typically solicits shareholder approval for director election and external auditor ratification. The former includes information about the individuals who serve or are nominated to serve on the audit committee and allows shareholder to withhold votes if they believe that certain members of the audit committee are not qualified. Such voting could also allow shareholders to withhold support for members of the nominating committee if they believe that such committee members have not been sufficiently diligent in selecting board candidates to serve on the audit committee. With respect to external auditor ratification, the audit committee report can describe the procedures followed by the committee in selecting the accounting firm to provide rationale to the shareholders for their approval.

While supporting a comprehensive audit committee report in the annual proxy statement, we also support continuation of the current SEC rule that requires registrants to either post a copy of the audit committee charter on their website or provide it as an appendix to its proxy statement at least every three years. It is useful to easily refer to such charters and we note that most registrants now provide them on corporate websites.

### **Encourage Voluntary Improvements Rather than Adopt Numerous Rules**

As noted earlier, there has been considerable improvement in the content of audit committee reports over the past five years or so. This has been due in large part to efforts such as *Enhancing the Audit Committee Report – A Call to Action*, issued by the Audit Committee Collaboration in October 2012 (Call). The Call provided a number of best practices in audit committee disclosures and many registrants have adopted those best practices and made other improvements. With appropriate encouragement from the SEC and perhaps others, we believe that this improvement trend will continue. We are concerned, however, that the numerous, very detailed questions in the Release may ultimately result in a number of quite specific proposals for both the format and the content of audit committee reports. We do not support extensive SEC rule making in this area as it is more likely to lead to a “check the box” or compliance approach leading to legalistic boilerplate rather than a more fulsome communication process.

We agree with the sentiment expressed in the statement on page 21 of the Release, “Others have suggested the need for principles-based reporting to allow for flexibility and to avoid a ‘one size fits all’ approach.” Of the 9,000 or so public companies, there is great variety in the size, nature, and complexity of operations. Equally so, the makeup of the audit committee activity of those registrants varies considerably and a standardized listing of requirements for all may not facilitate the most effective communication.

We do believe that general guidelines for audit committee reports are appropriate and would support the SEC’s publishing some. For our part, we believe the guidelines should be kept quite brief and broad. For example, we suggest that the basic objective of an audit committee report to be included in an annual proxy statement should be the following.



- To generally describe the committee’s most important responsibilities (with reference to the charter as appropriate).
- To describe the most important activities of the audit committee during the most recent year.

Some of the responsibilities and activities are those that are mentioned in the following sections of this letter.

### **Audit Committee Responsibilities Broader Than External Audit Oversight**

Of the 74 questions listed in the Release, only the last two questions deal with audit committee responsibilities other than oversight of the external auditor. The Release itself notes that “commenters may also provide views on other aspects of audit committee disclosures,” but hardly any attention is given to those “other aspects” in the Release. Yet, in practice, audit committees commonly spend more than a majority of their time at meetings and otherwise on matters other than oversight of the external auditors. Given that the large number of IMA’s members that are involved in financial reporting, we were particularly disappointed to see almost no attention given to the audit committee’s oversight of financial reporting and the internal controls over financial reporting.

While external auditing is an important part of the “checks and balances” to insure proper financial reporting to investors, the financial reporting function has the primary responsibility to “get it right.” The audit committee’s oversight responsibilities start by insuring that a registrant’s reporting systems and controls are strong and producing the proper information. That responsibility is clearly spelled out in audit committee charters and should be highlighted in annual audit committee reports as well. Committees could report on their procedures to review and comment on draft SEC filings and earnings releases, review significant new accounting policies, and oversee the testing of the internal control system. In short, an effective audit committee report should emphasize what the committee has done for the year to assure that financial reporting is accurate and internal controls are appropriate to the best of their understanding.

Comments in the report on the external audit function should focus on the non-routine matters that may be of most interest to investors. For example, the committee probably should summarize its reasoning for selecting the audit firm for which shareholder approval is requested, particularly if it is a change in auditors.

Beyond those matters, reports should cover the other important responsibilities that audit committees perform. This can vary from registrant to registrant but may include the following.

- Internal audit – Internal audit usually reports functionally to the audit committee. The committee reviews the annual audit plan, reads reports of completed audits, and must be consulted before the chief audit executive is hired or replaced.
- Employee hot line – Registrants must have systems for employees to report suspected misconduct including possible financial fraud. The audit committee usually reviews such reports.
- Legal and compliance – If a board does not have a separate compliance or similar committee, the audit committee will hold regular discussions with the general counsel, etc. covering these areas.



- Risk management – If a board does not have a separate risk committee or perform this duty at the board level, the audit committee will provide oversight of the company’s risk assessment and management, including cybersecurity.
- Information technology – Again, if a company does not have a separate technology committee, oversight of information technology often rests with the audit committee

Our point is not to list every duty that an audit committee may presently have but to highlight that generally most committees spend the majority of their time on matters other than oversight of external auditing. Thus, we strongly believe that any further action by the SEC be limited to general guidance that would suggest describing the general responsibilities of the committee, including references to the charter and describing the important activities during the current year in executing those responsibilities. “One size does not fit all” and we believe broad guidelines should be provided rather than detailed rules to enable meaningful disclosure.

**No Need to Report Normal Compliance Activities**

A number of the procedures performed by audit committees currently, whether pursuant to written rule or general practice, can be described as routine compliance. For example, the Release notes that Item 407(d) of Regulation S-K is no longer current because it references AU Sec. 380 rather than the current AS 16. The SEC may well want to make that updating correction at some point. But the larger issue is that stating in an audit committee report that “AS 16 has been complied with” is of no real usefulness to investors. Many of the matters in the Release fall into that same category. While it is appropriate for such procedures to be performed, it is more important to communicate to investors the audit committee’s work to assure that financial reporting is accurate and internal controls are appropriate than that the audit committee is doing what it is required to do by law. It would be a little like the external auditor’s listing of all their audit procedures in an auditors’ report when investors really are most interested to know if the auditors’ report is unqualified.

Thus, in keeping with our suggestion that any resulting proposals issued by the SEC be general guideline encouragements rather than detailed rule proposals, we urge that wherever possible the SEC avoid requiring reporting on matters that are routine compliance issues and limit reporting to material compliance exceptions.

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We would be pleased to discuss our comments with the SEC staff at their convenience.

Sincerely,

Nancy J. Schroeder, CPA  
Chair, Financial Reporting Committee  
Institute of Management Accountants

