
July 10, 2015

SEC Issues Concept Release Addressing Potential Changes to Audit Committee Disclosures

On July 1, 2015, the Securities and Exchange Commission (the “SEC”) issued a concept release seeking public comment regarding potential revisions to audit committee disclosure requirements, with a focus on the audit committee’s oversight of auditors. In the concept release, the SEC notes significant divergence in current audit committee reporting practice, together with investor concerns that current disclosure rules may result in disclosures about the audit committee that are not sufficient to help investors understand and evaluate audit committee performance and the auditor ratification process. The SEC is seeking comments to determine whether additional audit committee disclosure is warranted.

In the concept release, the SEC has solicited comment on three areas of audit committee disclosure:

- The audit committee’s oversight of the auditor, the audit and the auditor relationship;
- The audit committee’s process for appointing or retaining the auditor; and
- The audit committee’s consideration of the qualifications of the audit firm and members of the engagement team selected by the audit committee.

It is noteworthy that while regulators in other jurisdictions have in recent years focused on the role of audit committees and the relationship between public companies and their auditors (see, for example, the initiatives of the Financial Reporting Council in the United Kingdom), there has not been significant formal regulatory action affecting the role of audit committees in the United States since the promulgation of rules following the adoption of the Sarbanes-Oxley Act in 2002. In 2014, the SEC staff (see SEC Speaks, February 22, 2014, remarks of Paul Beswick, Chief Accountant, SEC Office of the Chief Accountant) warned registrants that it was expanding its focus on monitoring by audit committee of auditor independence and also in 2014 the SEC settled two enforcement actions against auditors for violations of independence rules. At the same time, audit committees have been strengthening their oversight, as part of their broader risk oversight activities, of compliance matters, in particular against bribery. The concept release is the culmination of SEC efforts to re-engage on the subject of audit committee roles.

The Audit Committee's Oversight of the Auditor

The concept release requests comments as to whether registrants should disclose additional information regarding actions the audit committee has taken to oversee the auditor and the audit. Potential additional disclosures include:

- Details regarding the nature and timing of communications between the audit committee and the auditor, including communications regarding overall audit strategy, timing and significant risks identified;
- A description of the frequency with which the audit committee met with the auditor;
- A review and discussion concerning the auditor's internal quality review and most recent PCAOB inspection report; and
- Whether and how the audit committee assesses, promotes and reinforces the auditor's objectivity and professional skepticism.

The Audit Committee's Process for Appointing or Retaining the Auditor

The concept release further requests comments on whether registrants should disclose additional information regarding the audit committee's process for appointing or retaining the auditor. Potential additional disclosures include:

- A discussion of how the audit committee assessed the auditor, including the auditor's independence, objectivity and audit quality, the audit committee's rationale for selecting or retaining the auditor and the audit committee's involvement in evaluating and approving the auditor's compensation;
- If the audit committee sought requests for proposal for the independent audit, the process the audit committee undertook to seek such proposals and the factors the audit committee considered in selecting the auditor; and
- The board of directors' policy, if any, for an annual shareholder vote on the selection of the auditor, and the audit committee's considerations of the voting results in its evaluation and selection of the audit firm, including situations where the audit firm fails to achieve majority support.

Qualifications of the Audit Firm and Certain Members of the Engagement Team Selected By the Audit Committee

The concept release also requests comments in respect of whether registrants should disclose information regarding the individuals on the audit engagement or other firms involved in the audit. Potential additional disclosures include:

- The name of the engagement partner and other key members of the audit engagement team, together with the length of time each team member served in that role and any relevant experience;
- The input the audit committee had in the selection of the engagement partner;
- The number of years the auditor has audited the company; and
- Information regarding other accounting firms or persons who are not employed by the auditor that performed audit procedures in the audit.

The SEC is also seeking public comment on whether audit committee disclosures should be part of registration statements and prospectuses in registered offerings and the application of audit committee disclosure requirements to smaller reporting companies and emerging growth companies.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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