

**MEMO# 29158**

July 9, 2015

## **SEC Concept Release Seeks Comment on Expanded Audit Committee Disclosures**

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TO: ACCOUNTING/TREASURERS COMMITTEE No. 18-15  
CLOSED-END INVESTMENT COMPANY COMMITTEE No. 15-15 RE: SEC CONCEPT RELEASE  
SEEKS COMMENT ON EXPANDED AUDIT COMMITTEE DISCLOSURES

The SEC recently issued a concept release seeking public comment on whether there would be benefit from requiring audit committees to provide additional audit committee report disclosure about their oversight of the independent auditor. [1] As you may know, closed-end funds are currently required to provide an audit committee report in their annual proxy statement. [2] Open-end funds, however, are not subject to the audit committee report requirement.

Among other things, the audit committee report must state whether the audit committee has: a) reviewed and discussed the audited financial statements with management; b) discussed with the independent auditor the matters required to be discussed by PCAOB standards; c) received the written disclosures and letter from the auditor required by PCAOB standards pertaining to the auditor's independence; and d) recommended that the audited financial statements be included in the shareholder report filed with the SEC. The Release asks whether additional disclosure about the audit committee's oversight of the independent auditor would assist investors in making investment decisions, or better inform proxy voting decisions regarding ratification of the auditor and the election of directors who are members of the audit committee.

Comments on the concept release are due to the SEC by September 8. The Institute and the Independent Directors Council are considering whether to file a comment letter on the Release. If you have any concerns with the Release, please let Jennifer Choi (202/326-5876, [jennifer.choi@ici.org](mailto:jennifer.choi@ici.org)) Greg Smith (202/326-5851, [smith@ici.org](mailto:smith@ici.org)) or Lisa Hamman (202/371-5405, [lhamman@ici.org](mailto:lhamman@ici.org)) know by August 7.

Current audit committee reporting requirements provide information about the role of the audit committee. These disclosures do not, however, describe how the committee executes its responsibilities. The Release notes that a significant number of audit committees voluntarily provide information beyond the disclosures required by the SEC's rules. According to the Release, this suggests that there may be market demand for such

information.

## **Potential Disclosures Discussed in the Release**

The Release requests public comment on possible disclosure changes primarily in three areas: the audit committee's oversight of the auditor; the audit committee's process for selecting the auditor; and the audit committee's consideration of the qualifications of the audit firm and certain members of the engagement team when selecting the audit firm.

### **Oversight of the Auditor**

The Release asks whether the SEC should require disclosure about the nature, timing, and frequency of communications between the audit committee and the auditor. For example, should the audit committee report on its communications with the auditor relating to the auditor's overall audit strategy, the significant risks identified, the nature and extent of specialized skills used in the audit, the results of the audit, and how the audit committee considered these items in its oversight of the independent auditor. Should the audit committee report disclose the frequency with which it met privately with the auditor?

The Release asks whether disclosure about the audit committee's review and discussion of the audit firm's most recent PCAOB inspection report and the audit firm's most recent internal quality control review would be helpful to investors. The Release asks whether the audit committee should disclose whether and how it assesses, promotes, or reinforces the auditor's objectivity and professional skepticism.

### **Process for Appointing or Retaining the Auditor**

The Release discusses possible disclosures about the process the audit committee undertook and the criteria used to assess the auditor and the audit committee's rationale for selecting or retaining the auditor. For example, if audit quality indicators are used in the evaluation of the auditor, should there be disclosure about the indicators used, including the nature, timing and extent of audit quality indicators considered by the committee?

Should disclosures include a description of the audit committee's involvement in approving the auditor's compensation, including how compensation is determined and evaluated? Should the audit committee provide disclosure about the nature and extent of non-audit services and its evaluation of how such services relate to its assessment of independence and objectivity?

The Release discusses possible disclosures about the number of audit firms that were asked to propose providing audit services, how those auditors were selected, and the information that the audit committee used in its decision to select the auditor.

### **Qualifications of the Audit Firm and Certain Members of the Engagement Team**

The Release asks whether the SEC should require disclosures about the length of the company's relationship with the audit firm and how tenure was considered in evaluating the auditor's independence and objectivity. Should the audit committee report name the engagement partner, the engagement quality reviewer, or their qualifications and experience? Where those individuals will rotate off the engagement in the upcoming audit, should that information be disclosed?

The audit committee may provide input into an audit firm's assignment of the individual who will serve as the engagement partner for the audit. Should the audit committee be

required to disclose what it considered in providing input to the firm's assignment of the engagement partner?

## **Mutual Funds**

Open-end funds are not currently required to provide an audit committee report and the Release does not specifically mention mutual funds. However, at question number 63 the Release asks:

"If the Commission were to proceed with requiring some or all of the disclosures proposed above, should the disclosures be made by all issuers? For example, should the disclosures be required only for those subject to the proxy rules? Should they be required for foreign private issuers? Why or why not? Should there be accommodations made for certain types of companies or certain circumstances? If so, what should they be?"

Gregory M. Smith  
Senior Director of Fund Accounting and Compliance

### **endnotes**

[1] Possible Revisions to Audit Committee Disclosures, Release Nos. 33-9982; 34-75344 (July 1, 2015) available at: <http://www.sec.gov/rules/concept/2015/33-9862.pdf> ("Release").

[2] Item 22(b)(16) under Schedule 14A of the proxy rules requires closed-end fund proxy statements pertaining to election of directors to include certain information relating to the audit committee. That information includes, among other things, the audit committee report required by Item 407(d) of Regulation S-K.