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August 3, 2015

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

File No. S7-13-15

Dear Secretary:

This letter represents my comments on the SEC's concept release (Release), "Possible Revisions to Audit Committee Disclosures." To provide some brief context for my comments, from 2001 through 2013 I served on five large public company boards and chaired the audit committee of each. I continue to serve on the board of directors of the National Association of Corporate Directors and in 2010 I co-chaired the Commission that developed the NACD Blue Ribbon Commission Report on the Audit Committee. Presently I am an Executive in Residence at the University of Georgia, having previously taught graduate level accounting classes for sixteen years. Before joining the UGA faculty I was Chairman of the Financial Accounting Standards Board for ten years and a senior partner with Ernst & Young for 26 years. While my comments in this letter are informed by all of those experiences, the comments are mine alone.

Overview

I am generally supportive of the SEC's initiative to improve the content of audit committee disclosures. While Section D of the Release asks certain questions about the location of audit committee disclosures in Commission filings, for purposes of this letter I will focus on audit committee reports that are included in annual meeting proxy statements as I believe such a single place for all such disclosures is preferable. For quite some time I have felt that a large portion of these reports failed to communicate the important work of companies' audit committees in an adequate manner. Whether because of legal concerns or other reasons, too many reports tend to be bland recitations of matters that aren't fully understood or of much relevance to investors. (Do investors really understand or derive any value from, "We discussed with the auditors all communications required by the PCAOB, including AS 16?") In effect, audit committees have been selling themselves short as they have been performing more and more important work on behalf of shareholders but failing to get their stories out. Audit committee members often complain about having too many matters assigned to them or simply being overworked. But average shareholders would never get that impression just from reading the audit committee reports in proxy statements.

While I support improvements to these reports, I am disappointed that in the Release the SEC has chosen to focus on the audit committee and auditor relationship. This is one of the important roles of audit committees but their responsibilities are much broader. The Release does go on to say that “commenters may also provide views on other aspects of audit committee disclosures, such as those related to roles and responsibilities, audit committee qualifications, oversight of financial reporting, or oversight of internal control over financial reporting.” However, of the 74 questions on which comments are requested, only the last two are directed to those “other aspects.”

As also noted in the Release, the Sarbanes-Oxley Act of 2002 defines an audit committee’s responsibilities as, “overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer.” The first part of that responsibility – oversight of the issuer’s accounting and financial reporting processes – is overlooked in this Release. Yet that is arguably an audit committee’s most important responsibility. Frankly, the very term, “audit committee,” is a misnomer. The body’s responsibilities should call for a broader title such as “accounting and auditing committee” or “financial reporting oversight committee.” In fact, with the far-reaching obligations of today’s committees, something even broader such as “external reporting oversight and compliance committee” might be a better descriptor.

So while I am very supportive of improving audit committee reports, I’m almost equally concerned that the narrow focus of the SEC’s concept release could have the (I hope not intended) outcome of requiring even more disclosures about the audit committee-auditor relationship. Thus, an already disproportionate and perhaps even misleading portrayal of audit committee activities would grow even worse. That would not be a positive outcome.

Rather than replying to all of the specific questions posed in the Release, this letter presents my views on what an audit committee report should generally endeavor to communicate, including a listing of specific matters. After providing that depiction of what I believe audit committees can and should communicate, I will comment on a few related matters.

A Suggested Outline for Audit Committee Reports

While audit committee reports have come a long way through efforts of the directors involved, with limited guidance from the SEC, the Audit Committee Collaboration¹, and others, in some respects they are still in an early stage of development. Therefore, I would hope that the SEC allows them to continue to develop largely as “best practices” without becoming overly prescriptive. If a long list of required contents is prescribed, these reports could become similar to today’s independent auditors’ reports that provide standardized language stating that compliance has occurred but failing to communicate very

¹ “Enhancing the Audit Committee Report – A Call to Action (Call)” (Audit Committee Collaboration, October 2012) provided audit committee report best practices examples and suggested that directors use them to evaluate and improve their own disclosures. I believe that was an important step in the evolution of these reports and note that many companies have made improvements since then based on the Call or on their own analyses. In general, I support the disclosures highlighted in the Call although, similar to the Release, the Call contains probably a bit too much emphasis on auditor-related matters.

adequately with investors and other users. At the other extreme, with absolutely no guidance, audit committees might regress to saying little or nothing, particularly if so cautioned by counsel. A middle ground should be sought where the SEC and/or others can provide reasonable guidance for the general content of an audit committee report without it becoming a check the box exercise. I agree with 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."

Accordingly, I believe the basic objective of audit committee reports should be to summarize a committee's important responsibilities and to describe how the committee has acted to meet those responsibilities for the past year. The emphasis should be on oversight of the financial reporting and internal controls as well as the independent auditing thereof. The report should also include the other important activities carried out by the committee but need not belabor routine compliance matters. Not every report will be similar as at least some audit committee duties differ from company to company. But with these very general guidelines in mind, the following are those matters that I believe should be considered for inclusion – to the extent they are relevant to a given company.

Scope of Duties – The first matter mentioned in the Call is the need for audit committees to clarify the scope of their duties. Companies are presently required to provide copies of the charter of the audit committee on their website and include copies in proxy statements periodically. Thus, audit committee reports should at least refer readers to the charter to make sure it is easy to locate. And I agree with the Call's suggestion that committees should consider including some discussion in their reports about the scope of duties. In particular, I think it is important for committees to consider mentioning duties that readers might not associate with "audit," such as risk management, legal compliance, and information technology, where appropriate.

Committee Composition – I also agree with the Call's recommendation that audit committee composition should be mentioned in the report. However, a mere listing of membership and statement that members meet the independence and financial literacy requirements provides no really useful insights. Rather, a description of why specified members have been determined to qualify as "audit committee financial experts (ACFE)" would be much more informative. See further comments about ACFEs later in this letter.

Oversight of Financial Reporting – As noted earlier, oversight of financial reporting is the primary responsibility of audit committees. While independent audits can add value to the financial reporting process, if a company's personnel and processes aren't doing things right in the first place it's a big problem. In my experience, the audit committee needs to and does spend considerably more time keeping tabs on company financial management (including internal audit, IT, and risk management) than on overseeing the external audit. Sufficient time was always spent on the latter but far more meeting time was devoted to the former. In speaking to groups of auditors, I always praised their work. But I told them that if there were an "Academy Award" for their efforts such as those for the motion picture industry, they would be entered in the "actor in a supporting role" category and not the "actor in a leading role" category as that would be reserved for management.

Given that perspective, I believe that audit committee reports should provide more information about what the committee does to ensure high quality financial reporting. Unfortunately, most audit committee reports I've seen tend to take a legalistic approach aimed at limiting committees' exposure for any deficiencies in the reporting. They emphasize management's primary responsibility for the financial reporting and internal controls as well as the auditors' responsibility for opining on them. The

audit committee oversight of financial reporting and controls is mainly described as discussions with the various parties. Sometimes even more limits are expressed such as the following from a company on whose board I formerly sat (Legg Mason), "The members of the Audit Committee rely, without independent verification, on the information provided to them and on the representations made by management and the independent auditors."

While I expect it will be difficult to convince legal advisors to reduce their concerns about wording in these reports, I would like to see audit committees be more forthright in describing this critically important activity. Ideally, reports should mention that, while management does have the primary responsibility for financial reporting and internal control, audit committees have:

- Read all 10-Ks, 10-Qs, annual reports to shareholders, earnings press releases, and earnings guidance releases in draft form and provided comments thereon to management,
- Reviewed significant accounting policies and disclosures on a regular basis, particularly any changes in accounting, as well as any material, unusual accounting items,
- Reviewed the testing of the system of internal control over financial reporting and the disposition of deficiencies, significant deficiencies, and material weaknesses identified,
- Reviewed the activities of the company's disclosure committee,

and then indicate that the committee has concluded, on the basis of the procedures performed, that those matters were handled appropriately to the best of the committee's knowledge. In sum, I believe that audit committee reports can do a better job of informing investors about the details of what they have done to ensure proper financial reporting and internal controls. And I further believe that, with the right caveats, committees can express more responsibility for what they have done and provide greater comfort to shareholders.

Oversight of Independent Audit – This area is, of course, the principal focus of the Release. Current audit committee reports devote a lot of attention to auditor-related matters and SEC action on the large number of questions in the Release could easily lead to even more such matters being required to be included. As stated earlier, I think this would be unfortunate as an overemphasis on auditor-related matters would give a misleading impression of what audit committees actually do. At the same time, this is an important responsibility and some matters clearly deserve reporting.

I do not think that reports need to cover all of the procedures that audit committees are required by law or regulation to perform. For example, a statement that the committee has received from the auditors the written disclosures required by applicable PCAOB rules, including AS 16, doesn't contain any useful information to investors other than that the committee "has done its job." In the extremely rare case where a committee hasn't done its job in such regard, the auditors presumably would need to report that as a material weakness in internal control.

Thus, matters relating to the auditor relationship should focus on those that have some possible incremental informational value to investors. The Call listed five auditor-related topics as leading disclosure examples – those that were emerging as voluntary disclosures that seemed to be useful. They are:

- Factors considered when selecting or reappointing an audit firm.
- Selection of the lead engagement partner.
- Factors considered when determining auditor compensation.
- How the committee oversees the external auditor.
- The evaluation of the external auditor.

I believe the first item should be included in all audit committee reports. After all, the report commonly accompanies a proxy statement vote for shareholders to ratify the appointment of the audit firm. Thus, the report should always devote at least a couple of sentences to describing the committee's process. In the past this process may have been perfunctory in many cases. The audit committee may have reasoned along the lines of: X firm has been our audit firm for 25 years, we haven't had any problems with them and the fee seems fair. I hope that the reappointment process, including appropriate evaluation, is becoming much more rigorous. In any event, disclosing what the committee has done will inform investors about the care given to the decision.

I am not as concerned about disclosing the process re: selection of the lead engagement partner. As noted later, I do not support disclosure of the name of the engagement partner and, therefore, describing the selection process seems unnecessary to me. Selection of the audit firm is where the attention and full disclosure should focus, in my view.

Likewise, I don't see much value in describing how the committee determines auditor compensation. Any such disclosures are likely to be quite general and it isn't clear what investors would do with the information beyond what they do with the fee amounts already reported in proxy statements.

Oversight and evaluation are related and do represent topics that warrant mention in audit committee reports. Again, these disclosures are likely to be somewhat general in content but perhaps over time seeing what various committees are doing to oversee and evaluate will lead to improvements in these activities.

Risk Assessment and Risk Management – New York Stock Exchange listing requirements specify that audit committees must discuss guidelines and policies to govern the processes by which a company's exposure to risk is managed. The audit committee is not required to be the sole part of the board responsible for risk assessment and management and many companies have separate risk committees or assign this responsibility to the full board. Similar to financial reporting, the primary responsibility for risk assessment and management rests with management. But board oversight is very important and this topic is high on the list of priorities at many companies. As such, a description of the audit committee's role in risk assessment and management would be an appropriate part of any report.

Information Technology – Again, some companies have information technology or just technology committees that would have oversight responsibility in this area. But audit committees are quite commonly assigned oversight responsibility. This has become a particular hot button recently with all of the attention being paid to cybersecurity. Investors should be interested in reading about what audit committees do to oversee the efficacy of a company's information technology.

Internal Audit – Similar to the risk area, New York Stock Exchange listing standards require the audit committee to oversee the internal audit function. Reports should describe the audit committee's oversight of the internal audit function, including the committee's role in the appointment of the chief audit executive. This could include comments on approval of internal audit's annual audit plan and review by the committee of the results of completed audits.

Legal and Compliance – Unless the board has a separate compliance committee, this is another area usually assigned to audit committees. The audit committee report could mention the committee's discussions with legal counsel, compliance officials, and other individuals with respect to matters that need to be accounted for or disclosed in SEC filings or other public reports.

Other Matters – Audit committees have other duties prescribed by law or regulation such as making sure that the company has established procedures for the confidential submission by employees of concerns about questionable accounting or auditing matters. And some audit committees have been assigned responsibility by their boards for other matters such as reviewing related party transactions or officer expense accounts. I see no need for those “routine” responsibilities to be regularly included in the audit committee report. I think investors should assume that the committee has performed the tasks assigned to it in its charter and the annual report should focus on matters such as those listed above that are of the most interest. 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. Eventually, the SEC will want to fix that inaccuracy but rather than simply replacing AU 380 with AS 16, I urge consideration of whether continuation of this rule is even necessary.

With reference to AU 380, AS 16, and similar matters, I urge the SEC to refrain from requiring audit committees to include references to specific rules and or to state similar conditions that are only understandable only to technical accountants and auditors. Any guidelines provided by the Commission for audit committee reports should stress that they be written in plain English and in a way that reasonably informed investors can appreciate.

Disclosure of the Name of the Engagement Partner

Question 34 asks in part, “Whether disclosure of the name of the engagement partner would be useful to investors?” My opinion is that it would not. A separate PCAOB project has been studying whether the name of the engagement partner should be disclosed in the auditor’s report. And recently the PCAOB issued a supplemental request for comment asking whether disclosing that name in a form filed with the PCAOB would be a better approach than including it in the auditor’s report. For reasons detailed in my January 6, 2014 and July 17, 2015 comment letters to the PCAOB (available on the Board’s website), I have opposed this PCAOB initiative. Briefly summarizing my position:

- Disclosing a name provides no useful information. It would require development of a system to accumulate facts about an individual. Neither the PCAOB nor investors have done an adequate job of determining what such a database should include, how the information would be developed, and who would pay for it. Further, there is no compelling evidence that any resulting information would actually affect investment decisions in the marketplace.
- Supporters argue that disclosing the engagement partner’s name would increase her or his “accountability.” Yet the current environment that subjects engagement partners to firm independent partner review, firm quality control review, PCAOB inspection, SEC review, and civil litigation already creates such a high level of accountability that it is virtually impossible to see that there could be a higher level in practice. Further, adopting such a requirement is likely to lead to a reduction in the pool of qualified engagement partners as the slightest “negative taint” on an individual would cause audit committees to reject them as engagement partners. This could also lead to qualified individuals leaving the profession as the threat of a negative event occurring (a restatement beyond their control or frivolous litigation about financial reporting) could end their careers at any time.

As stated in my most recent letter to the PCAOB, if the SEC determines that disclosure of the name of the engagement partner does provide useful information, I believe the disclosure should be made in annual meeting proxy statements and not in the auditors’ report or a PCAOB form. An even better alternative would be to leave this matter up to the discretion of audit committees. If they felt it would be useful to investors, they could include it in their reports in the proxy statement. If enough investors

pushed for this, it could then become common disclosure in such reports and the world could see if the databases envisioned by the PCAOB would, in fact, ever develop.

Audit Committee Financial Expert

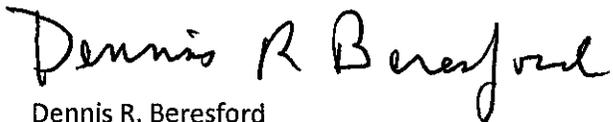
Question 74 of the Release asks, in part, "Should the Commission consider the potential for changes that would affect the role and responsibilities of the audit committee, such as those related to qualifications of members of the audit committee ...?" In response I urge the SEC to revisit the definition of an Audit Committee Financial Expert. More specifically, I believe the inclusion of the language "or experience actively supervising one or more persons engaged in such activities" has resulted in too many individuals being classified as ACFEs who do not have the necessary accounting and auditing knowledge. While audit committees can benefit by having a diversity of backgrounds among their membership (assuming basic financial literacy among all), a good committee ought to have at least one member who can actually "speak GAAP and GAAS" (have a very good understanding of generally accepted accounting principles and auditing standards). Rather than belabor the issue in this letter, I have attached an article I co-authored on this topic several years ago that I believe is still quite timely. Making this amendment to SEC rules would actually make them more consistent with the Sarbanes-Oxley Act of 2002 and I urge that you take this up soon.

Conclusion

An effective audit committee can help ensure that a registrant's filings with the SEC are accurate and all of its accounting and auditing activities are performed in an appropriate manner. Committees should do their best to communicate with investors and other interested parties about the important work they are accomplishing. The SEC concept release can lead to further improvements in the reports that audit committees issue but it is essential that they be balanced in their content and not overly emphasize audit-related matters or any other single responsibility.

Thank you for considering these comments and I would be pleased to answer any follow up questions you may have.

Sincerely,



Dennis R. Beresford
Executive in Residence

Attachment – "How 'Expert' Is Your Financial Expert?" from the February 2005 issue of *Directorship*

Copyrighted material redacted. Author cites:

Beresford, Dennis R., and Joseph Hinsey. "How 'Expert' Is Your Financial Expert?" *NACD Directorship*; Feb. 2005, Vol 31, Issue 2, p. 10.