In discussing audit committee oversight, reporting and the broader dialogue between companies and investors on accounting and audit issues, our three speakers covered the following areas:

The investor-audit committee relationship:
The investor-audit committee relationship is a developing one though it may have got off to a rocky start. It could be argued that the audit committee role has long been overlooked by an investor community that has traditionally placed greater emphasis on the remuneration committee. "The audit committee has suffered with being the poor relation on the board." Daniel Summerfield observed that in his view, the investor community had been "slow to recognise and engage with audit committees". With audit committees facing new challenges and increased expectations, new regulation is forcing a change in this dynamic.

Impact of regulation
Regulatory change has not been without its challenges – not least, the tensions created around mandatory rotation and tendering. Daniel reflected on how views around the benefits of regular tendering and rotation have evolved in the past five years. Historically there was a commonly-held view among preparers and auditors that mandatory rotation and tendering was "an expensive bureaucracy with little added value". Now views are changing with many of those who have been through an audit tender now recognising that whilst the process can be expensive and time-consuming, it has not resulted in "the Armageddon predicted". It was also noted that whilst the recent audit reforms have not really resulted in enhanced choice in the audit market, it is "hard to defend companies with one hundred years of audit tenure". In respect of regulatory changes to reporting, Daniel shared some insights from recent corporate governance studies which suggest that audit committee reports are showing improvements in the detail provided about how the audit committee discharges its duties, and where they have challenged the financial statements. [Notwithstanding the positive trends in reporting, the recent FRC Lab Report notes that there is still room for improvement in this area – see box below]

Reporting of audit committees
The 2015 FRC Lab Implementation study ‘Reporting of Audit Committees – How companies responded to investor needs identified by the Lab; experience of the first year’ looks at the audit committee reports of 34 companies from across the FTSE 350 and makes the following recommendations:

— Style of the audit committee report – Overall, companies have implemented the Lab’s findings well, but personalising the report by adding the audit committee chair’s photo and signature would go further to meet investor preferences based on building the perception of accountability.

— Significant financial reporting issues – Improvement is recommended for the majority of companies in relation to the depth and quality of explanations. Also, to meet investor expectations, detailed explanations of considerations by the audit committee in relation to accounting judgements and estimates (not only impairment considerations which are often disclosed) could be included.
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Other projects

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The format, where four different questions were debated
partners, audit committee chairs, auditors and investors.

Aerospace and Defence sector, including lead audit
accountancy firms, and 20-30 representatives from the
PRG activity, involving the largest six

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get their annual reports to be understood by people who
not trained accountants. The audit committee’s role in

ensuring that the annual report is fair, balanced and
expected audit tender date.

— Safeguards on non-audit services – Audit
committees have been reporting on this area for

— Appointing the auditor – While audit committees
suggestions in this area, there is still room for

— Assessing external auditor effectiveness – Most
companies have significant room to improve
reporting in this area, by providing more detail on
the activities undertaken and each of their
outcomes.

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The Implementation Study can be found here:

Level of dialogue/insight demanded by investors and analysts

Whilst regulators have pointed to investor needs as the
rationale for many of the recent governance changes, this
sense was less prevalent amongst the investors present at
the breakfast. Providing an analyst’s perspective, Deborah
Taylor noted that, unless there is a known problem, analysts
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The Investor Forum

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launched in October 2014, and was set up by the
investment industry to foster better relations between UK
 corporates and their owners. The intention of the Forum is
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accountancy firms, and 20-30 representatives from the
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partners, audit committee chairs, auditors and investors.

The format, where four different questions were debated
by the group, provided “an amazing combination of practical
learning, highlighting the different views that companies
can take on issues like audit materiality”. Other projects
that The Investor Forum are involved in include Banking
Future, being launched in February 2016, which looks at
long-term culture change.

Ten points that emerged from the subsequent Q&A and discussion:

1. Is the commonly-held view that Investors want more
from their relationships with audit committees a
misconception? And how much has this view driven
regulation? Does the investment community really
value many of the new disclosures required to be
included in audit committee reports? One attendee
remarked, “I don’t believe investors lead this – the
regulators are the ones driving it!”

2. Many of the attendees had experienced very little
interaction with investors so far and acknowledged
that this could be improved further. One attendee
commented that “any interaction with investors would
be a start! Only one person has interacted in six
years”, and another remarked that a suggestion
offered for the audit committee chair to speak to
investors had been met with “a resounding silence”.
Conversely, it was recognised that the level of
investor-audit committee engagement needs to
achieve the right balance. There is the danger of going
too far and ending up with “US-style regulation and
frequent, aggressive meetings”.

3. Is a lack of interaction always a bad thing? It was
noted that this could be seen as a positive indicator
and it might be “comforting that there are not queues
of people wanting to talk to audit committee chairs”.

4. Audit committee chairs are on the “frontline of
governance” but a lack of interaction with investors
can leave an audit committee feeling “untrusted”. Andy
Griffiths noted that boards should be seen and
presented as one of a company’s most important
assets, but this is rarely the case. The Investor Forum
wants to “champion investors thinking of the board as
an asset”.

5. One attendee noted that board level communication is
exceptionally valuable to investor insight. It conveys
a strong sense of the corporate culture and operating
style – something that cannot be achieved by only
talking to a CEO or CFO. The current narrow focus
can, and should be improved by ensuring the
investment community engages with more people
from across the entire board.

6. Boards should think about which investors to engage
with, and consider focusing on those “intrinsic
investors who are staying with the company for the
long-term”. Similarly, smaller investment portfolios
might allow investors to spend more time getting to
know companies deeper (and for the longer term).

7. Is there an expectation gap around the audit
committee ‘role’, and does there need to be more
pragmatism across the wider business community as
to what an audit committee can reasonably be
expected to do? The media is quick to shine the
spotlight on non-executive directors, and the audit
committee in particular, when things go wrong. But is
it always reasonable to expect audit committee
oversight to prevent all business failures? While it was
accepted that in some cases audit committees could
have done better, it was also noted that in the case of
some notable so-called corporate failings, the audit
committee would have had to be very exceptional to
have picked up on what was going on much deeper in
the organisation.
8. When considering the circumstances under which investors and audit committees should be communicating, one attendee noted that “one area we found that investors wanted to interact was around audit rotation and tendering. It seemed to be a good point to start the dialogue. It was raised in the regular annual meeting with the audit committee and remuneration committee”. Another suggestion was that “audit committee chairs could sit in on the roadshow, just to observe the CEO, see how the debate flows, what people ask about and who turns up, rather than experience what might be a synthesised view fed back by the executive”. Some attendees reported that they do this already.

9. Lessons might be learned from the interactions between remuneration committee chairs and the investor community. Usually specific agenda items are covered as meeting objectives and act as “hooks”. If meeting agendas are pushed out in advance, this might create an opportunity for the audit committee chair to attend existing scheduled ‘investor’ meetings instead of, or in addition to the Board Chairman.

10. The onus is also on investors to ensure that the right people represent their franchise in any significant meeting with audit committees (or other Board members). Whilst it may not be feasible for senior individuals to attend every meeting, equally, replacing a senior individual with a junior ‘governance’ person is not always appropriate either.