January 5, 2015

The Organisation for Economic Co-operation and Development
2, rue André-Pascal, 75775 Paris Cedex 16
Via dafca.contact@oecd.org

Re: 2014 Review of the OECD Principles of Corporate Governance

Dear Sir or Madam:

The Center for Audit Quality (CAQ) is an autonomous public policy organization dedicated to enhancing investor confidence and public trust in the global capital markets. The CAQ fosters high quality performance by public company auditors, convenes and collaborates with other stakeholders to advance the discussion of critical issues requiring action and intervention, and advocates policies and standards that promote public company auditors' objectivity, effectiveness, and responsiveness to dynamic market conditions. Based in Washington, D.C., the CAQ is affiliated with the American Institute of CPAs (AICPA).

The CAQ appreciates the opportunity to comment on the Organisation for Economic Co-operation and Development's (OECD) proposed changes to its *OECD Principles of Corporate Governance* (the "Principles"). Our comments are specifically focused on the proposed changes to Section V, *Disclosure and Transparency*, of the Principles. This letter represents the observations of the CAQ, but not necessarily the views of any specific firm, individual, or CAQ Governing Board member.

We agree with certain proposed changes to Section V of the Principles, which reflect an increased emphasis on auditor independence and call for additional disclosures of Board and committee structures and charters. However, we believe that the auditor independence section overall could be updated and strengthened.

We believe the shared understanding that a high level of transparency, accountability, board oversight, and respect for the rights of shareholders and role of key stakeholders is part of the foundation of a well-functioning corporate governance system. The CAQ further believes that any enhancements to the Principles should be principles-based to adapt to the continuing evolution of the corporate sector and capital markets. In particular, we believe that changes to the Principles should:

- Support and enhance the role of the audit committee in meeting its important responsibility to protect the interests of shareholders in relation to a company's financial reporting and internal controls, which in turn, contributes to audit quality;
- Provide appropriate flexibility to avoid a "one size fits all" approach to the wide range of company and board situations; and
- Take into consideration the implications for various major markets, given that consistency across jurisdictions is an important goal.

Auditor Independence

Stakeholders, including those with roles within corporate governance, continue to rely on high-quality, objective audits to provide reasonable assurance that a company's financial statements are presented fairly. The external auditor should be independent, both in fact and in appearance, and we support the OECD proposed change to expand on the importance of auditor independence in the Principles by stating, "The independence of auditors and their accountability to shareholders *should be required*."[1] However, we encourage the OECD take a more principles-based approach and delete the list of specific examples of "other provisions to underpin auditor independence,"[2] because it includes measures that may not work consistently across different legal and regulatory environments.

Further, while audit firms ultimately are responsible for maintaining their independence and delivering high-quality audits, effective governance mechanisms—including independent audit committees[3] and independent audit regulation—provide the foundation for and reinforce enhanced audit quality. Therefore, we agree with the added statement that "the designation of an audit regulator independent from the profession can be an important factor in improving audit quality,"[4] and believe other factors such as the oversight of the auditor by the independent audit committee also contribute to enhanced audit quality.

Enhanced Audit Committee Transparency

Effective audit committees help ensure financial reporting integrity by means of their oversight responsibilities. Audit committees can underscore their effectiveness by clarifying their responsibilities for overseeing financial reporting and the independent audit, including the independence of the auditor, through increased transparency. We therefore commend the OECD for clarifying within the Principles that "it is *good practice* for external auditors to be *recommended by an independent audit committee* of the board or an equivalent body and to be appointed either by that committee/body or by shareholders directly."[5] We believe a similar requirement in the United States, where all members of the audit committee of a public company must be "independent" of the company, its directors and controlling shareholders,[6] greatly adds to their ability to oversee the financial reporting processes of a company and the external auditor in an objective manner and free from undue pressure from management.

Further, audit committee transparency can promote greater investor confidence in financial reporting and the external audit by providing stakeholders with a greater understanding of the audit committee's oversight role. In recent years, companies in various countries have begun to disclose more information

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[1] Page 27, Section V. Disclosure and Transparency, *OECD Principles of Corporate Governance*.
[2] Page 28, Section V. Disclosure and Transparency, *OECD Principles of Corporate Governance*.
[3] The term "audit committee(s)" includes those charged with governance of financial reporting, internal controls and the audit, in recognition of diverse language and legal structures around the world. To the extent that some jurisdictions might use a different terminology to describe bodies that serve the same purpose, the term "audit committee(s)" would apply to those bodies, as well.
[4] Page 28, Section V. Disclosure and Transparency, *OECD Principles of Corporate Governance*.
[5] Ibid.
[6] Final Rule 33-8220, *Standards Relating to Listed Company Audit Committees*.

about their audit committees' oversight responsibilities, generally going beyond the minimum required by country law or stock exchange rules. In some cases this has been driven by changes in regulatory requirements, while in other cases it has been driven by enhanced stakeholder interest. For instance, the Audit Committee Collaboration's[7] *Enhancing the Audit Committee Report: A Call to Action* encouraged public company audit committees "to voluntarily and proactively improve their public disclosures to more effectively convey to investors and others the critical aspects of the important work that they currently perform."[8] The CAQ supports the OECD's increased emphasis on transparency by calling for disclosures of Board structure, including committees.

The CAQ also supports enhanced language calling for the required disclosure of fees for non-audit services, as such disclosure contributes to the transparency of services provided by auditors that may impact their independence. Further, this language is generally consistent with the rules of the Securities and Exchange Commission (SEC), which require public companies to disclose in their proxy statements the total fees paid to the external auditor within four categories: audit, audit-related, tax, and other, along with a discussion of pre-approval of non-audit services.[9] Further, a best practice is to include a discussion in the proxy statement of how non-audit services may impact independence. For instance, as noted within *The Audit Committee Transparency Barometer*, the CAQ's joint publication with Audit Analytics, "83% of S&P 500 companies, 69% of S&P MidCap companies, and 58% of S&P SmallCap companies discussed how non-audit services may impact independence in their audit committee reports and/or other sections of the proxy statements."[10]

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In closing, auditor independence and increased transparency around the oversight responsibilities of audit committees are essential to the quality of financial information provided by companies, and further contribute to audit quality and increased investor confidence. Because of the importance the role audit committees play in supporting the integrity of financial reporting, the CAQ encourages consistency in the development of guidance for audit committees across global markets and stands ready to help support such efforts with the audit committee community in the United States.

The CAQ supports the OECD's efforts to ensure the continuing high quality, relevance and usefulness of the Principles and appreciates the opportunity to comment on changes to Section V, *Disclosure and Transparency,* of these Principles. We would be pleased to discuss our comments or answer any questions that the OECD may have regarding the views expressed in this letter.

Sincerely,

Cynthia M. Fornelli
Executive Director
Center for Audit Quality

[7] Several nationally recognized U.S. governance organizations came together to collaborate on projects intended to leverage their efforts to expand the spectrum of public companies to strengthen audit committee performance and transparency. Known as the Audit Committee Collaboration, one of these projects was *Enhancing the Audit Committee Report: A Call to Action*, published in November 2013.
[8] Page 4, *Enhancing the Audit Committee Report: A Call to Action*
[9] Final Rule 33-7919, *Revision of the Commission's Auditor Independence Requirements*.
[10] Page 5, *2014 Audit Committee Transparency Barometer*.