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January 15, 2016

Marlice Johnson
International Corporate Governance Network
6-10, Saffron House, Kirby St,
London EC1N 8TS,
United Kingdom

Re: ICGN Global Stewardship Code: *Member Consultation*

Dear Ms. Johnson:

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, DC, the CAQ is affiliated with the American Institute of CPAs (AICPA).

The CAQ welcomes the opportunity to comment on the International Corporate Governance Network (ICGN) Member Consultation on the *Global Stewardship Code* (the Code). This letter represents the observations of the CAQ, but not necessarily the views of any specific firm, individual, or CAQ Governing Board member.

The CAQ supports and shares the ICGN's goal to promote effective standards of corporate governance worldwide and views investor stewardship as a potentially effective mechanism for reinforcing good governance and transparency through enhanced engagement between those acting on behalf of shareholders and the companies in which they invest. Institutional investors, as the dominant owners of listed companies in many developed markets, are positioned to hold members of management and the board accountable for faithfully discharging their fiduciary responsibilities to shareowners and investors.

I. General Views

While enhancing investor confidence is central to the CAQ's mission of building trust in global capital markets and fostering high quality public

company auditing, the CAQ itself is not an investor and as such is not in a position to comment on the specific principles and guidance points proposed in the Code. However, broadly speaking, the CAQ supports the principles-based and non-prescriptive approach ICGN has taken in drafting a framework that can be tailored to accommodate specific situations. In addition to providing flexibility to avoid a “one size fits all” approach to the wide range of investor circumstances, the principles-based framework of the Code promotes global consistency in investor stewardship while allowing for jurisdictional differences in approaches needed due to differences in legal environments and cultural norms.

The CAQ believes that accountability, board oversight, and respect for the rights of shareholders are fundamental to a well-functioning corporate governance system. Boards should provide meaningful information to investors about how it executes its responsibilities, which would enable investors to monitor and respond, if necessary, to urge closer harmonization of board strategy with investor expectations. Disclosures by investors made in relation to the Code regarding their major stewardship approaches, can assist companies to understand these approaches and the expectations of their major shareholders.¹ The potential result is better alignment of corporate and shareholder interests and improvement in long-term value creation at the company and risk-adjusted returns to shareholders.

II. Benefits of Transparent Investor Engagement with Investee Companies

Effective corporate governance is a multifaceted concept involving many checks and balances, and a tone at the top that emphasizes competence and integrity. Internal checks include three lines of defense – (1) operating management; (2) risk, control, and compliance functions in support of management; and (3) internal audit.² Executive and non-executive directors are charged with fiduciary duties to oversee these control functions on behalf of investors. Increasingly, investor stewardship codes are being implemented or considered to establish areas of good practices investors can demonstrate to fulfill their responsibilities as asset owners, or stewards, on behalf of the ultimate beneficiary. ICGN’s Code, for example, provides guidance points regarding investor engagement with companies in which they invest “to build mutual understanding and promote responsible governance practices.”³ The Code also encourages investors “to disclose their major stewardship priorities and forward-looking engagement strategy.”⁴

While investors do not require a stewardship code to engage with management and the boards of the companies in which they invest, the CAQ sees potential benefits flowing from transparent engagement by investors with investee companies, as envisioned by the Code. For investors who choose to actively engage, following the principles and guidance set forth in the Code will add transparency to those activities. Through our outreach, research, and other efforts, the CAQ has heard from representatives of corporate boards and management of companies that they want to engage with investors about their informational needs.

¹ See p. 11 of the Code.

² The Institute of Internal Auditors, *Leveraging COSO across the Three Lines of Defense*, July 2015. Available at <http://www.coso.org/documents/COSO-2015-3LOD-PDF.pdf>.

³ See p. 10 of the Code.

⁴ See p. 11 of the Code.

III. Enhanced Audit Committee Reporting May Facilitate Investor-Audit Committee Engagement

From an audit and audit committee perspective, enhanced investor interest and attention to the board's activities reinforces board accountability and therefore should fortify processes for board oversight of financial reporting and the audit process. The potential result is a continuing cycle of mutually reinforcing activities that bring about increasingly beneficial outcomes in terms of board effectiveness and quality financial reporting.

Over the last few years, the CAQ has partnered with ICGN to hold panel discussions with investors and audit committee members around the world.⁵ Much of those discussions have focused on the challenges that impede more frequent and meaningful investor and audit committee engagement. We have learned from these discussions that there are practical reasons why investor engagement with the audit committee, as well as with management and the full board, of investee companies, is infrequent. We heard that in many cases, engagement activity is either absent or tends to focus on a narrow range of issues or the voting process at the Annual General Meeting.

On the other hand, panelists have indicated that upward trends in enhanced reporting by audit committees in various countries have led to more engagement between investors and audit committees. Indeed, a key impetus behind the U.K. Financial Reporting Council's requirements that expanded audit committee reporting was to encourage more frequent and meaningful engagement between investors and audit committees.⁶ In some cases enhanced audit committee transparency has been driven by changes in regulatory requirements, while in other cases it has been driven by enhanced stakeholder interest.

In the United States, research conducted by the CAQ in partnership with Audit Analytics indicated double-digit growth from 2014 to 2015 in the percentage of S&P 500 companies disclosing information in several key areas of auditor oversight.⁷ The Audit Committee Collaboration,⁸ of which the CAQ is a member, encourages public company audit committees of all sizes and industries to voluntarily and proactively improve their public disclosures to more effectively convey to investors the critical aspects of the important work they perform.⁹ The CAQ believes that enhanced audit committee reporting could facilitate more meaningful engagement between investors and investee companies.

IV. Conclusion

⁵ Transcripts from these discussions are available at <https://www.icgn.org/information/highlights>.

⁶ Financial Reporting Council, Guidance on Audit Committees, Sept. 2012. Available at <https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Guidance-on-Audit-Committees-September-2012.pdf/> The changes to the Code made in 2012 introduced requirements for audit committees to provide more detail on the work they do, including: descriptions of the significant issues considered by the audit committee in relation to the financial statements and how they were addressed; how the audit committee assessed the effectiveness of the external audit process; and their approach to appointing the auditor and safeguarding objectivity and independence relative to the use of non-audit services.

⁷ See the 2014 and 2015 Audit Committee Transparency Barometer, both available at <http://www.thecaq.org/reports-and-publications/audit-committee-transparency-barometer>.

⁸ 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. For more information, visit <http://www.auditcommitteecollaboration.org/>.

⁹ Enhancing the Audit Committee Report: A Call to Action (2012), available at http://www.auditcommitteecollaboration.org/EACD%20Case%20Study_v19.pdf.

The CAQ supports the concepts embodied in the Code to increase investor transparency and meaningful engagement with companies and views it as a potentially effective mechanism for promoting effective corporate governance. We believe that increased transparency can facilitate open dialogue between investors, corporate boards, and management, and, in turn, reinforce accountability and good governance practices. We also believe that greater transparency from investors regarding their informational needs will provide helpful feedback to audit committees and enable them to focus the financial reporting of the company and the audit committee's disclosures on addressing investor questions and concerns. This could inspire more frequent and meaningful investor and audit committee dialogue, which could work to focus audit committees on ensuring that their activities are serving the investors they represent.

The CAQ appreciates the opportunity to comment on the Membership Consultation and would be pleased to discuss our comments or answer any questions that the ICGN may have regarding the views expressed in this letter.

Sincerely,

A handwritten signature in black ink that reads "Cynthia M. Fornelli". The signature is written in a cursive, flowing style.

Cynthia M. Fornelli
Executive Director
Center for Audit Quality