BoardroomDirect

The monthly newsletter for PwC's Center for Board Governance – August 2012

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Breaking news

SEC issued final rules on conflict minerals disclosure on August 22. Click here for a CFOdirect publication on the new rules.

Issues in brief

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Latest Center for Board Governance publications

The quarter close - Directors edition Q2 2012 focuses on the FASB's and IASB's decision on lease accounting, the implementation of the JOBS Act, and feedback on PCAOB's proposed mandatory audit firm rotation concept release.

Worth reading

Analysis of ISS Negative Recommendations Against Directors
Failure to act on shareholder proposals led to withhold votes.
- *Corporate Board Member*

CalPERS, CalSTRS, GMI Ratings launch board diversity tool
Diverse Director DataSource helps companies seek candidates.
- *Corporate Secretary*

Center for Board Governance Webcast

The September 13 Center webcast will focus on the results of our Annual Corporate Director Survey. For more information and to register, click here.

Board Governance Series

In an interview with Corporate Board Member, Tom Craren, PwC managing partner of brand and thought leadership, discusses the firm's 15th annual CEO Survey. Click here.

Contact us

For more information about this newsletter, contact Gary Larkin (gary.p.larkin@us.pwc.com).

Issues in brief

Audit firm inspection reports – what they mean for audit committees

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The Sarbanes-Oxley Act, which recently marked its 10th anniversary, created the Public Company Accounting Oversight Board (PCAOB) - the regulator of the public company auditing profession in the United States. One of the PCAOB's important duties is to annually inspect the largest accounting firms that audit public company financial statements.

PwC's *10minutes on audit committee effectiveness* notes a leading practice for audit committees is to "learn from the results of the auditor's internal and external regulator quality inspections." The publication also points out that if auditors do not initiate discussions about these inspections and reviews, i.e., both internal inspections conducted by the audit firm itself and those conducted by the PCAOB, audit committees should. **[For more details, read BoardroomDirect June 2012.]**

On August 1, the PCAOB released a document: *Information for Audit Committees About the PCAOB Inspection Process*. It outlines inquiries that an audit committee should consider making of its audit firm about the firm's inspections. It also contains information to help audit committees understand the inspection process. The PCAOB makes the point in its release that information regarding inspection results can have value for an audit committee not only in relation to the audit committee's oversight and evaluation of the audit engagement generally, but also in relation to the audit committee's role in the oversight of the company's financial reporting process. **[Click here to read the PCAOB's statement on the release.]**

PwC welcomes the PCAOB's outreach to audit committees with this release. We believe it can be helpful in facilitating robust dialogues between audit committees and auditors about audit quality in general, in addition to relevant quality indicators, including PCAOB inspection results. We also believe it will be helpful for audit committees to understand the investments firms are making in continuous quality improvements at a high level as well as engagement specific enhancements based on quality indicators.

We will continue to address the important topic of audit quality in upcoming issues of *BoardroomDirect*.

Board declassification, majority voting top proxy issues

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Corporate governance proposals seeking board declassification, adoption of a majority voting requirement, and the elimination of supermajority voting requirements were the most successful in the 2012 proxy season, according to recent reports. At the same time in its second year the number of failed advisory

Say on Pay votes increased while the number of directors targeted for removal decreased.

According to The Conference Board's *Proxy Voting Fact Sheet* issued on August 1, the largest number of proposals filed at Russell 3000 companies as of June 30 related to corporate governance (352 proposals). Of those, approximately 66% were voted upon, 28% were omitted from the proxy statement by management, and 3% were withdrawn by their sponsors.

Among corporate governance shareholder proposals, board declassification (which would result in all directors being up for election annually) was the most popular, averaging 80% "for" votes. Other widely supported proposals were the elimination of supermajority voting requirements (68%) and the adoption of majority voting in director elections (61%), The Conference Board reported.

Among shareholder proposals on social and environmental policy, support level remained consistently low despite increased volume, according to The Conference Board. Political issue-related proposals received an average "for" vote of less than 20% among the 70 that were included in proxy statements. Thirty-two environmental issue proposals also received "for" votes of less than 20 percent.

Support for executive compensation proposals remained about the same in 2012 compared to 2011 with nearly 98% passing and 92% receiving more than 70% support. However, the number of failed executive compensation proposals increased to 53 from 40, according to a Sullivan & Cromwell report on Say on Pay.

The Conference Board reported that although the number of failed Say on Pay votes increased in 2012, the total number of compensation-related proposals geared toward directors decreased to 63 (less than half of the volume in 2009 and 2010). Of those proposals, there appeared to be more focus on the introduction of retention periods for equity-based awards (26 of the 63 proposals, up from 14 proposals in the January 1 to August 3, 2011 period) and limiting golden parachutes and other severance agreements perceived as extravagant (12 of the 63 proposals, up from 7 in the 2011 period).

For more information on the 2012 proxy season, view an archive of PwC's Center for Board Governance Proxy Insights and Trends webcast.

Group issues virtual shareholder meeting guidelines

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For companies holding or thinking about holding virtual annual shareholder meetings, a best practices working group led by the institutional investor CalSTRS published *Guidelines for Protecting and Enhancing Online Shareholder Participation in Annual Meetings* **[Read the press release here.]**

The Best Practices Working Group for Online Shareholder Participation in Annual Meetings comprises retail and institutional investors, public company representatives, and proxy and legal service providers. The group published the report in June to make companies aware of safeguards that should be in place during virtual-only and hybrid shareholder meetings. (A virtual-only meeting refers to one where shareholders can participate only through online technology while a hybrid is where the in-person meeting is broadcast to remote shareholders).

The 12-page report includes sections on principles, best practices, and relevant laws and listing standards. Three principles the group adopted are:

- **Safeguards for online participation in shareholder meetings:** Companies holding online shareholder meetings should not use technology to "avoid opportunities for dialogue" that would otherwise be available at an in-person meeting.

- **Online participation in shareholder meetings should maximize the use of technology:** That includes offering telephone access to shareholders so they can ask questions, ensuring accessible technology for webcasting for different platforms, providing technical support, and opening web sites and telephone lines in advance of the meeting to allow shareholders to test their access.

- **Cost benefit analysis:** Companies should consider the cost and benefits of holding a physical meeting vs. a virtual-only meeting or a hybrid meeting, and the rights of shareholders.

For a synopsis of the report, read The Harvard Law School Forum on Corporate Governance and Financial Regulation blog post from the working group.

Audit committee issues

FASB seeks input on disclosure framework

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As part of its efforts to improve the effectiveness of disclosures in financial statement footnotes, the Financial Accounting Standards Board (FASB) has proposed a disclosure framework.

The FASB believes that establishing a framework for disclosure is a first step before it can make any specific changes to existing disclosure requirements. It then plans to use the framework to possibly modify existing disclosure requirements and write new ones.

"Many stakeholders have expressed concerns about the relevance and sheer volume of information in notes to financial statements, and that some information is either missing or difficult to find," FASB Chair Leslie F. Seidman said. "Therefore, the FASB is looking to improve its own procedures for establishing disclosure requirements and to provide a way for reporting organizations to exercise judgment about which disclosures are relevant to them."

In its invitation to comment, the FASB addresses such topics as:

- A decision process to help the standard-setter establish disclosure requirements that address relevant information
- Flexible disclosure requirements that could be adapted by each reporting organization (company) to focus on relevant information
- A judgment framework that could help each reporting organization determine which disclosures are relevant
- Organization and formatting techniques that could make the information users need easier to find and understand.

Those seeking to comment are urged to do so by November 16.

The FASB will hold an educational webcast on Wed. Sept. 5, 2012 from 1-2 p.m. EDT entitled *IN FOCUS: The FASB Disclosure Framework Project.*

For more information on the FASB disclosure framework invitation to comment, read PwC's *In brief: FASB solicits input on ways to improve disclosure effectiveness*.

FASB explores a revised impairment model for financial assets

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The FASB earlier this month decided not to go forward with the so-called "three bucket" impairment model for financial assets. Instead, it will explore a revised approach.

A recent PwC *In brief: FASB decides to explore a revised impairment model for financial assets* spells out the three bucket model as well as the revisions the standard-setter will consider. Under the three bucket impairment model, financial assets would initially be placed in “bucket 1,” where credit reserves would be established for only those assets expected to experience a loss event in the next 12 months. As credit risk deteriorates, assets would then move to “bucket 2” or “bucket 3,” where credit reserves would be based on a lifetime of expected losses, irrespective of when the loss event is expected to occur.

The board considered whether implementation guidance could adequately clarify the objectives of the model. The board concluded that even with improved definitions for the key terms, there would likely still be concern over whether the model results in credit reserves that faithfully represent the credit risk of the portfolio. As a result, the board directed its staff to explore a model that incorporates the concept of expected losses, but applies that concept to all financial assets held and uses a single measurement approach.

The FASB hopes to share its findings with the International Accounting Standards Board in early fall.

Resources, webcasts and events

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Center for Board Governance Webcast: The September 13 Center webcast will focus on the results of our Annual Corporate Director Survey. The webcast will take place 2-3 p.m. ET. For more information and to register, click here.

Board Governance Series, Vol. 21 2012: This issue of the Corporate Board Member magazine includes an interview with Tom Craren, PwC managing partner of brand and thought leadership, on the results of the firm's 15th annual CEO Survey, titled "Growth and Value in a Volatile World." Other articles in this volume include executive compensation challenges in a volatile economy and digital volatility and director literacy. **To read the Series, click here. To watch the video, click here.**

Women in the Boardroom Webinar: Catherine Bromilow, a partner in PwC's Center for Board Governance, will speak on "What You Need to Know to Get into the Boardroom and Be Successful in the Boardroom" at a Women in the Boardroom webcast at noon ET on September 14. The webinar will address hot issues facing directors, how to effectively deal with directors and the skill sets boards need the most. For more information, click here. To register, click here.

Board of Directors Forum: Strategy & Risk: The board's role in striking a balance (Minneapolis): Please join us for a board of directors forum on Tuesday, October 2, 2012 from 7:30 – 10:00 a.m. in Minneapolis, MN. The breakfast and networking session will include a discussion of the Board's role in corporate strategy and risk oversight. Ample time will be allotted for Q&A and a facilitated peer discussion. Please contact Kelly Sutherland (kelly.r.sutherland@us.pwc.com) for more details and to RSVP.

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