

## Current issues for boards of directors



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Directors are increasingly using electronic portals and tablet devices to access board materials and books, and the trend is likely to continue.

### Proxy access: Not gone yet

Directors don't have to worry about mandatory proxy access for the 2012 proxy season, thanks to a decision by the US Court of Appeals for the District of Columbia Circuit. In July, the court struck down the Securities and Exchange Commission's proxy access Rule 14a-11, which was authorized by the Dodd-Frank Act in 2010.

The court's recent decision in *Business Roundtable et al v. Securities and Exchange Commission* stated that the SEC "acted arbitrarily and capriciously" by failing to adequately assess the costs and benefits of Rule 14a-11. The court also said the SEC failed to prove its claim that the rule would improve shareholder value and board performance. The rule would have allowed shareholders owning at least 3% of a company's stock for at least three years to include their nominees for directors in the company's proxy at the company's expense—this could have made it much easier for shareholders to oust directors.

Directors may believe that the issue has now been settled, but the debate over proxy access is certainly not over yet. In fact, many now believe the focus will shift to the SEC's Rule 14a-8 amendment, which could revive the battle on a company-by-company basis.

Also called "private ordering," the amendment to Rule 14a-8 was introduced when the Commission adopted Rule 14a-11 in August 2010. Originally, Rule 14a-8 allowed a company to exclude from its proxy materials any shareholder proposals related to director elections. But the amendment precludes a company from excluding shareholder proposals relating to director nominations. Shareholders would first need to submit a proposal to change the company's bylaws to allow proxy access. If successful, they could then in the subsequent year propose their own director nominees for inclusion in the company's proxy materials.

The Commission stayed the implementation of both Rule 14a-11 and the Rule 14a-8 amendment after the challenge to proxy access was filed in September 2010. The SEC originally said that the 14a-8 amendment was complementary to and "intertwined" with Rule 14a-11. But in a statement following the ruling, the SEC pointedly noted that the amendment was "unaffected by the court's decision."

## Examining mandatory audit firm rotation

The PCAOB release outlines 21 specific questions regarding engagement term length, the scope of a potential engagement, and transition and implementation considerations.

The mandatory audit firm rotation debate is back. In August, the Public Company Accounting Oversight Board (PCAOB or “board”) issued a concept release requesting comments on ways it could enhance auditor independence, objectivity and professional skepticism. It included the possibility of imposing mandatory audit firm rotation, a subject that has been proposed several times since the 1970s as a way to increase auditor independence.

The debate stems from the fact that auditors are paid directly by the companies they audit and often have long-standing relationships with them. Mandatory rotation would limit the number of consecutive years that a public company could use the same registered public accounting firm to serve as its auditor.

The PCAOB is soliciting comment on the idea of mandatory audit firm rotation. The board is also seeking feedback on whether other measures could enhance auditor independence, objectivity and professional skepticism. The release outlines 21 specific questions regarding engagement term length, the scope of a potential engagement, and transition and implementation considerations. It summarizes some of the arguments on this topic.

### Advocates for rotation

- Have expressed the need for increased auditor independence, particularly after the recent financial crisis. They say mandatory rotation would enhance the auditor’s ability to act as an independent gatekeeper.
- Believe a rotation requirement would help reduce the pressure auditors can face from clients and company management.
- Believe that auditor term limits would allow auditors to focus on

investors first, above their long-term relationships with clients.

- Say that a fresh viewpoint of a company’s financial statements by new audit firms would help protect investors.

### Critics of rotation

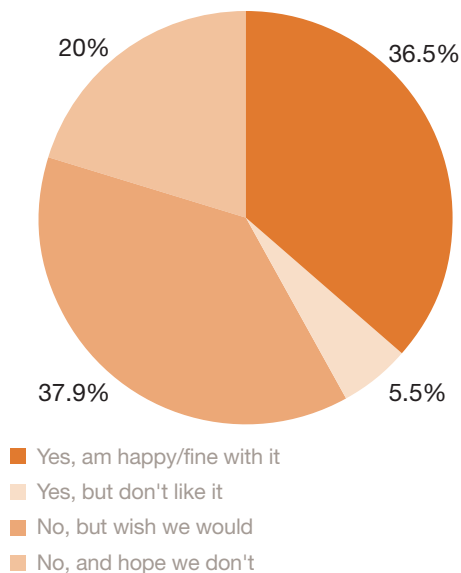
- Believe that audit quality would suffer in the first years of an engagement, as the new auditor learns about a company’s business, systems, and processes.
- Are concerned about the time companies will incur and the costs they, and ultimately their investors, will incur, in getting the new auditor up to speed.
- Note that mandatory rotation would not allow audit committees to consider any specific facts or circumstances relevant to changing auditors and could result in audit committees having to choose among firms with less industry expertise.
- Point to the possibility that rotation might obscure internal company problems, as well as problems between a company and its auditor.

Mandatory rotation would directly impact audit committees and boards. Thus, the concept release provides an important opportunity for constructive dialogue between the PCAOB and key stakeholders in the financial reporting system. Input from audit committees and board members will be especially critical to inform the PCAOB’s perspective.

We encourage audit committee members and other directors to express their views. Comments are due December 14. The board will convene a public roundtable meeting about mandatory audit firm rotation and independence in March 2012 to further consider the input it receives through the comment letter process.

## Technology storms the boardroom

In the last 12 months, has your board begun to use tablets, smartphones, and/or other mobile devices for board-related information delivery?\*



\*PwC's 2011 Annual Corporate Directors Survey

The digital age has made its way into the boardroom.

Many companies now offer their boards access to private electronic portals and secure intranets, and many issue tablet devices to their board members and executive management. These emerging technology trends are both innovative and popular, and many directors and companies have embraced them as ways to increase efficiency and effectiveness in the boardroom.

Nearly 50% of directors said that their boards had a secure intranet location where they could access board materials, according to PwC's 2010 Annual Corporate Directors Survey (ACDS). That's almost double the 28% who had such access in 2006.

One reason the use of online board portals has surged is the introduction of electronic tablet devices. Tablets have become very popular with directors—they are lighter and more portable than laptops, which mobile directors appreciate.

More than 36% of directors surveyed in PwC's 2011 ACDS said their board has begun to use tablets and other mobile devices for board-related information in the past 12 months. Nearly 38% of directors polled said they don't use tablets but hope they will. The remaining 26% of directors either don't like tablets or don't want to use them. (Official 2011 survey results will be released in October—check [PwC's Center for Board Governance website](#) to learn more.)

Directors can avoid backaches by using portals and tablets—both give directors access to internal company documents, eliminating the need for weighty paper board books and associated delivery logistical challenges. These technologies also allow companies to produce and deliver materials to their boards more quickly and more often,

with the flexibility to provide any important or relevant updates in real-time. Directors can even use portals to vote on board issues by electronic signature.

Often, the relevant technology is an outsourced solution, so company management and boards must take care to choose the best provider for their needs and ensure the system is secure.

While these new technologies may make directors' lives easier, it is also important for boards to be aware of the risks involved, as cyber-attacks and security breaches increasingly present problems for companies. The material contained within a company's online portal is highly sensitive and often includes inside information, so directors should ensure the company understands how the portal vendor provides security and who is liable for a security breach.

It may also take time for directors to fully adapt to the new technology, so companies should look for a platform that will be easy to use. Some directors prefer a portal that mimics hard-copy board books so the electronic transition is easier. Often, training is provided to help ease the transition, and many companies designate an employee as a liaison to the board to help with any issues.

PwC's Center for Board Governance has also stepped into the tablet scene with its [PwC Board Center](#) app available for the Apple iPad. The app provides updates on corporate governance issues and other content targeting directors, including information about financial reporting, executive compensation, risk management, and strategy and growth.

## Proxy access: Not gone yet

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In early September, the SEC said it would not appeal the court ruling. As a result, the stay on the Rule 14a-8 amendment expires when the court's ruling is finalized, which is expected on September 13. This opens the door for proxy access through private ordering. Directors can prepare for this possibility by:

- Anticipating an increase in the number of proxy access proposals—shareholders would only need \$2,000 in company stock and to have held it for one year.
- Reviewing company bylaws and amending them to include more robust advance notice mechanisms and conditions for shareholder nominations.
- Identifying any internal issues relating to director nomination or board composition, including reviewing the company's nominating committee charter, bylaws relating to director qualifications, rules for the conduct of shareholder meetings, and the policy on director age and term limits.
- Ensuring that there is regular shareholder engagement to identify and address concerns related to director nominations.

Proxy access under the Rule 14a-8 amendment is not an easy proposition, but boards should not count it out.

### How PwC can help

To have a deeper discussion of how these subjects might affect your company or board, please contact:

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### You may also want to see

**Audit Committee Effectiveness—What Works Best, 4th edition** is now available. This book is a practical guide, providing information and best practices on topics that are most relevant to help audit committees enhance their performance and effectiveness. The 4th edition has been updated to emphasize global practices and it incorporates survey trends, allowing you to understand how audit committees are responding to the various challenges they face. Visit our website to receive your complimentary copy. [www.pwc.com/us/ace](http://www.pwc.com/us/ace).

#### NACD BoardVision, featuring PwC

PwC's Center for Board Governance is participating in an on-demand webcast series designed to educate directors and C-suite executives on current issues that impact their strategic and operational decisions. "NACD BoardVision" features PwC partners discussing these issues. Episodes may be viewed at [www.nacdonline.org](http://www.nacdonline.org).

For these and other PwC corporate governance publications, visit the Center for Board Governance at <http://www.pwc.com/us/centerforboardgovernance>.