October 31, 2017

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Inside this edition

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PwC's 2017 Annual Corporate Directors Survey

The Global State of Information Security Survey 2018

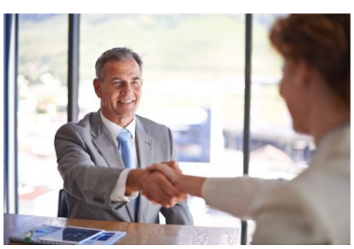
Only 44% of respondents say their corporate boards actively participate in their companies' overall security strategy. Massive cybersecurity breaches have become almost commonplace, regularly grabbing headlines that alarm consumers and leaders. But for all of the attention such incidents have attracted in recent years, many organizations worldwide still struggle to comprehend and manage emerging cyber risks in an increasingly complex digital society.

The Essential Eight technologies – Board byte: the internet of things

The IoT is one of the biggest disruptors for companies across industries. As more devices connect to the internet and to one another, it's moving beyond consumer devices to businesses of all kinds. The IoT creates opportunities for new products, services and business models. Boards should understand how this technology will impact their company's strategy.

CII's The audit committee in action: Simulated response to a whistleblower

In order to show the inner workings of the audit committee, CII hosted a breakout session co-led by PwC and the CAQ at the 2017 Fall Conference that featured a simulated response to a whistleblower who alleges fraud.



PwC's Corporate Directors Exchange

Specifically designed for directors of Fortune 1000 companies, this program will allow you to gain insights and share ideas with a network of peers and specialists who will help you navigate the future with confidence. You will also get perspectives straight from the country's top corporate directors, activist investors, a senior member of the SEC and other industry and Firm leaders. This complimentary event, hosted in New York, Palm Beach and San Francisco, has been called "the best seminar of its kind" by past attendees. Space is limited—register today.

Events and education

Join our team for engaging discussions at these upcoming governance events:

Equilar Chairman and lead director peer exchange

New York, NY
November 2, 2017

Palo Alto, CA
November 13, 2017

Join GIC leader, Paula Loop, as she discusses board composition.

Stanford Institutional Investors Forum (SIIF)

Palo Alto, CA
November 7, 2017

Join GIC leader, Paula Loop, as she discusses investor governance hot topics.

University of Southern California and NACD Corporate Director Symposium

Los Angeles, CA
November 8, 2017

Join GIC managing director, Paul DeNicola, as he moderates a roundtable on nominating and governance committee issues.

Main articles

SEC approves new PCAOB auditor's reporting model

The SEC approved new rules and amendments related to the auditor's reporting model that were proposed by the PCAOB earlier this year. The guidance is the result of a multi-year PCAOB effort that began in 2010. The new standard retains the existing "pass/fail" opinion, but makes significant changes to the form and content of the auditor's report for public companies. Additionally, starting in 2019 for certain audits, auditors will be required to communicate critical audit matters (CAMs) in their reports.

"CAMs are designed to provide investors and other financial statement users with the auditor's perspective on matters discussed with the audit committee that relate to material accounts or disclosures and involved especially challenging, subjective or complex auditor judgment," says Jay Clayton, SEC Chairman.

Certain provisions, including those requiring disclosure of auditor tenure and changing the form and standardized wording of the auditor's report, are effective for audits of fiscal years ending on or after December 15, 2017.

Insights and actions

The new standard will result in the first significant changes to auditor reporting in over 70 years. Similar changes have been made in recent years to auditor reporting in other countries. Audit committee members should be discussing the effect of the newly-approved standard during their upcoming meetings. It will be important for the audit committee to understand the changes to the current year audit report, such as how auditor tenure is determined. Many companies already disclose auditor tenure in audit committee reports generally contained in proxy filings. We believe audit committees are best placed to consider whether the length of the auditor's tenure may negatively affect audit quality, based on their direct interaction with auditors. Accordingly, in this environment, audit committees may wish to consider the sufficiency of proxy disclosures around audit committee oversight of auditors, including its considerations related to auditor appointment and retention. Looking ahead, it will be important to understand how CAMs are identified and the auditor judgements involved. The communication about CAMs among management, the audit committee and the external auditor will also be imperative. For an overview of the approved standard, see PwC's *In depth*. For additional information, watch PwC's US Chief Auditor, Len Combs, discuss the approved standard in this video.

PwC issues 2017 Annual Corporate Directors Survey results

PwC released the results of its *2017 Annual Corporate Directors Survey*, which captured feedback from nearly 900 public company directors. The survey covered a spectrum of governance topics, such as board composition and effectiveness, board diversity, shareholder engagement and activism, to name a few.

The top 6 findings are:

- **Missing the mark in the boardroom**: Forty-six (46) percent of directors indicated that one or more of their fellow board members should be replaced. This is an increase from 35% in 2016.
- **Diversity in the boardroom**: Eighty (80) percent of female directors indicated that diversity in the boardroom is happening too slowly, compared with just 33% of male directors.
- **Executive pay**: When asked whether executives are overpaid, 70% of directors at least somewhat believe that executives are overpaid. Sixty-six (66) percent at least somewhat believe that executive compensation exacerbates income inequality.
- **Shareholder engagement**: Forty-two (42) percent of directors say that someone on their board other than their CEO engaged directly with shareholders. Almost one-quarter of directors (23%) think that board members simply should not meet with shareholders. But more and more, shareholders have come to expect director engagement.
- **Disconnect on ESG**: Forty (40) percent of respondents indicated that climate change should not be taken into account when creating company strategy. Thirty (30) percent of directors say they don't have ESG/sustainability expertise and don't need it. However, in 2017, ESG issues, such as climate change, gained traction with investors. For the first time, shareholder proposals that focused on environmental issues passed at S&P 500 companies, with average support for climate change shareholder proposals jumping from 24% in 2016 to 32% in 2017.

- **New demands on boards**: Emerging technologies are a challenge for boards. Eighty-six (86) percent of directors say that new technologies are challenging to oversee.

CAQ releases 2017 Key Audit Considerations

The Center for Audit Quality (CAQ) released their *Select Audit Considerations for the 2017 Audit Cycle*, detailing some of the more judgmental or complex audit areas. Some of those complex areas were identified by the PCAOB in a recent Staff Inspection Brief.

Some of the topics described in the report include auditor independence, multinational audits and financial reporting, such as going concern and income tax accounting and disclosures. In addition, the publication highlights the following:

Transitioning to the new accounting standards:

- The CAQ details procedures auditors are reminded to perform, including reviewing SEC Staff Accounting Bulletin (SAB) No. 74 (codified in SAB Topic 11.M) disclosures to evaluate the adequacy of disclosures in both interim reviews and audits prior to adoption of a new accounting standard. The accounting standards' required disclosures may result in a significant change to footnotes, even if they do not have a significant impact on the primary financial statements.
- The CAQ reminds auditors of their responsibility to assess factors that affect the risk of material misstatement, to design audit procedures as appropriate and to assess if companies have adequate controls in place to address the disclosures of new standards. Auditors should consider if there have been any material changes in Internal Control over Financial Reporting (ICFR) due to the adoption of new standards, which may warrant disclosure in the annual or interim reporting periods.

Cybersecurity risks

- The PCAOB will look to understand if engagement teams updated their risk assessments and audit procedures in response to cybersecurity risks.

ISS' 2017–2018 Policy Application Survey results released

Institutional Shareholder Services Inc. (ISS) released the results of its *2017–2018 Policy Application Survey*, highlighting responses to topics such as executive compensation and the gender pay gap in the US. This was the second in a two-part survey conducted by ISS this year. The first, *The Global Policy survey*, summarizes the findings on a limited selection of governance topics (see summary in the October 3rd newsletter). The *Policy Application Survey* is more expansive and geographically diverse.

ISS received 328 responses to its latest survey, of which 77 were institutional investors. The rest were non-investors. Of the 328 responses, more than 200 were from the US, 55 from Europe and/or the UK and 30 were from Canada.

The survey addressed topics such as outcomes-based compensation measures, non-employee director pay, gender pay gaps and poison pills. For example, 60% of investors and 17% of non-investors in the US indicated that companies should be disclosing gender pay gaps. For additional detail, refer to the full survey results.

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