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AUDIT COMMITTEE AND AUDITOR OVERSIGHT UPDATE

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Summary

2022 PCAOB Large Firm Inspection Reports. The PCAOB has made public the 2022 inspection reports for the U.S. affiliates of the six global network audit firms. (The version of KPMG's report that the PCAOB released was not complete in that the Board redacted discussion of one engagement.) Overall, the inspection results for these firms declined in 2022, compared to 2021 and 2020. In 30 percent of the six firms' inspected engagements, the PCAOB found one or more Part I.A deficiencies – that is, deficiencies of such significance that it appeared that the firm did not obtain sufficient evidence to support its opinion. (The KPMG redaction does not affect this percentage.) All six firms had a higher percentage of inspected engagements that were deficient than in 2021. While the upward trend in deficiencies is concerning, the 2022 results are not dramatically out of line with the six firms' past performance. Nonetheless, the firms need to consider and address the root causes of the increasing number of inspection deficiencies.

Audit committees should discuss their audit firm's inspection report with the engagement partner. Audit committees may want to understand how the auditor addressed, or plans to address, engagement deficiencies highlighted in its report and whether the report will result in any changes in audit procedures that could affect the company's audit. If the company's engagement was the basis for an inspection finding, the audit committee should understand the cause of the deficiency and how the auditor plans to remedy it and prevent a recurrence. (more)

SEC Adopts Landmark Climate Change Disclosure Rules. On March 6 – almost two years after publishing its initial proposal – the SEC adopted final rules requiring public companies to make extensive disclosures concerning climate change. Among other things, the rules require most large accelerated filers and accelerated filers to disclose information about their material Scope 1 and Scope 2 greenhouse gas emissions and to obtain an assurance report with respect to those disclosures from a qualified, independent third party. In addition, all public companies will be required to disclose in their financial statements the capitalized costs, expenditures, charges, and losses incurred as a result of severe weather events and other natural conditions, such as hurricanes, tornadoes, flooding, drought, wildfires, extreme temperatures, and sea level rise. These financial statement disclosures will be subject to de minimis thresholds, generally tied to one percent of net income or stockholders' equity. The climate disclosure rules will be phased in, starting for large accelerated filers with fiscal years that begin in 2025.

For most companies, implementing the SEC's climate disclosure rules will require significant changes to information-gathering processes, internal controls, and disclosure review. Management, the audit committee, and the full board should begin considering now what steps the company will need to take to comply. The Update suggests questions that audit committees might ask as they begin their oversight of the implementation of the SEC's climate-related disclosure regime. (more)

Cybersecurity and ERM Are Top Audit Committee Priorities. ESG, Not So Much. The Center for Quality and the Deloitte Center for Board Effectiveness have released their third annual survey of audit committee practices and priorities, Audit Committee Practices Report: Common Threads Across Audit Committees (2024 Practices Report). As was the case last year, cybersecurity and enterprise risk management topped the list of audit committee concerns. Finance and internal audit talent was third. Environmental, social, and governance reporting, the third-highest concern last year, fell to sixth place, and 11 percent of respondents said that their audit committee spent too much time on ESG. In terms of ways of improving audit committee practices and effectiveness, "increased discussion and/or engagement from members during meetings" and "improved quality of pre-read materials" were the two most frequent suggestions. Many survey respondents also thought their committee would benefit from additional cybersecurity expertise. (more)

Ceres Advocates Climate Disclosure Reasonable Assurance. Ceres, a nonprofit organization that works with capital market leaders to address sustainability challenges, has released Closing the Gap: Investor Insights into Decision-Useful Climate Data Assurance. The report explores the challenges investors face in obtaining reliable and rigorous climate-related information and highlights the need for independent, third-party assurance to validate the credibility of corporate sustainability reports. Ceres suggests steps that companies and assurance providers can take to afford investors greater confidence in climate data disclosures. Several of these suggestions are aimed at audit committees. Among these, Ceres recommends that the audit committee oversee all climate-related assurance providers and be involved in determining the type, scope, and procedures of these engagements. Ceres also urges companies to "phase out or reduce" the use of reports that provide only limited assurance and instead obtain reasonable assurance over their climate disclosures. (more)

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The Update's website is www.auditupdate.com.

Update Nos. 89-present (March 2024 to present) and summaries are available here. Update Nos. 76-88 (August 2022 to February 2024) and summaries are available here. Update Nos. 60-75 (June 2020 to July 2022) are available here. Update Nos. 49-59 (January 2019 to May 2020) are available here. Updates prior to No. 49 are available on request.

An index to titles and topics in the Update beginning with No. 39 (July 2017) is available here.