



NORGES BANK
INVESTMENT MANAGEMENT

Secretary
Securities and Exchange Commission
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Response to the SEC concept release on possible revisions to audit committee disclosures

We commend the SEC for seeking public comment on audit committee reporting and whether the audit committee should provide more qualitative disclosures on how it has fulfilled its oversight function.

Norges Bank Investment Management (NBIM) appreciates the opportunity to provide perspectives and comments to the Securities and Exchange Commission's (the SEC) release no. 33-9862 of 1st July 2015 on possible revisions to audit committee disclosures ("the concept release").

NBIM is the investment management division of the Norwegian Central Bank and is responsible for investing the Norwegian Government Pension Fund Global (GPF). At 30 June 2015, the fund was invested in assets of 6,897 billion kroner (880 billion US dollars) with approximately 184 billion US dollars invested in equity of more than 2,100 listed US companies.

We support strong corporate governance practices at national and market level, as well as adherence to recognised international standards of corporate governance. We consider the UN Global Compact, the OECD Principles of Corporate Governance and the OECD Guidelines for Multinational Enterprises to be important points of reference for best corporate governance practises for all the markets in which we invest.

NBIM has previously responded to a number of the SEC's consultations, among them being our response to the 2009 release on proxy access and the 2010 release on the US proxy system.

Through this letter we will give our principled views on some of the issues that we find key to the audit committee's role with respect to its oversight role.



Executive summary

We believe effective and transparent audit committee oversight to be very important to investor protection. Increased transparency and disclosure on the committee's work, is likely to make audit information more relevant and useful to investors and can provide a stronger foundation for a well-functioning financial market. We believe international alignment of audit and audit committee reporting would benefit investors in an environment where markets, companies and investors have become increasingly global.

Increased transparency may help investors act as considered owners, i.e. assessing company boards and management and the strategies adopted for the longer term. Such transparency can also be useful for shareholders when voting on auditor ratification and election of audit committee members.

The audit committee should communicate effectively how it actively oversees the financial reporting process. The reporting should include information on how the committee has assessed and discussed the most challenging and contentious aspects of the financial reporting, the quality and independence of the external auditor, as well as how it has ensured a direct and regular relationship with the external auditor.

Audit committee reporting requirements must be crafted carefully to avoid boilerplate reporting. The information disclosed must be relevant, informative and detailed, but a balance must be struck to avoid a state of "disclosure overload".

Alignment with international changes and developments

There is considerable variability in audit committee responsibilities and disclosure requirements across the more than 70 markets in which NBIM has investments. As observed by the SEC, audit committees reporting practises also differ across companies within a single market, like the US.

We acknowledge the SEC for considering international developments in its work and referring to regulative initiatives on audit committee reporting and strengthened audit regulation that has emerged internationally¹. We believe international alignment of audit committee reporting would benefit markets, companies and investors that all have become increasingly global². We understand that differences in regulatory and listing requirements and corporate governance guidance naturally will be a driving force behind regulation in each jurisdiction. Keeping this in mind, we will at the same time encourage the SEC to continue emphasising international alignment in its further work.

The oversight role and accountability towards shareholders

Shareholders and regulators in the global capital markets have increasingly focused on the role of the audit committee and its accountability in discharging its duties, especially with respect to the financial

¹ As the International Auditing and Assurance Standards Board's acknowledgement of the positive impact on audit quality of enhanced audit committee disclosure and the amendments to the Directive on Statutory Audit adopted by the European Union in April 2014.

² NBIM is a member of the International Corporate Governance Network who supports the Global Disclosure Guidelines for Audit Committees Reports, prepared by the Enhanced Disclosure Working Group in 2011.



statement audit³. The audit committee should communicate effectively to shareholders and investors whether it has received sufficient, reliable, and timely information from management and the external auditors for it to fulfil its oversight responsibilities.

The audit committee should explain how it has challenged the work of the external auditor and thereby lend confidence to the quality of the audit and the credibility of the financial reporting. The audit committee reporting should emphasise how key risks and audit issues have been managed. Reasonable assurance should be given on how any control and risk related issues raised by the external auditor have been addressed.

The audit committee must show in which ways it assumes direct responsibility of the oversight of the external auditor. It should be clear how it exercises its authority to hire, compensate, oversee and, if necessary, terminate the auditor. The audit committee should disclose how it has discussed and evaluated the independence of the auditor. The reasons for a change of external auditor should clearly be set out as well as the reasons for renewing the engagement of an auditor with long tenure, tight relationships to the company, or any known substantive deficiencies.

Shareholders should be able to ratify the external auditor at the annual general meeting. The audit committee should disclose how it seeks dialogue with investors and how it has solicited the views of shareholders concerning the external auditor.

Evaluation and training of the audit committee members

All members of the audit committees of US listed companies must be financially literate and independent, and at least one member must qualify as a financial expert⁴. Despite these requirements, audit committees most times have members who have far less training or experience than the individuals whom they oversee, yet they are expected to challenge them.

It should be disclosed if and how the audit committee members receive regular training to ensure they keep abreast of auditing, accounting, and relevant risk issues. In view of the significant complexity of some accounting and auditing standards, specialised training should be obtained when appropriate.

Process of and conclusions from a regular audit committee evaluation should be reported, including an assessment of the skills, competences and experiences of the committee members and how this blend fits the specific challenges of the company. It should be disclosed who carried out the evaluation and any input and assessment from the external auditor on the duties and operational effectiveness of the audit committee should be disclosed.

³“Global Observations on the Role of the Audit Committee - Summary of Roundtable Discussions”, 2013, the Federation of European Accountants, the Institute of Chartered Accountants.
<http://www.fee.be/component/content/article.html?id=1330:fee-icaa-and-caq-global-observations-on-the-role-of-the-audit-committee-a-summary-of-roundtable-discussions>

⁴ As directed by the Sarbanes-Oxley Act of 2002, adopted by SEC rule 10A-3 and the listing rules of the national securities exchanges.



Increased disclosure on the communication with the external auditor

The audit committee should explain how it has ensured a direct and regular relationship with the external auditor. Tight cooperation and communication will better inform the audit committee, in particular on critical audit matters. Steps taken to ensure regular communication independent from management should be explained⁵.

Processes and activities to oversee the external auditor should be clearly set out. The audit committee should explain how it has discussed with the external auditor the terms of the audit engagement and the auditor's responsibilities. Such discussions should include the overall audit strategy, what kind of specialized skills and knowledge is required to perform the planned audit, as well as if and how external parties are used. Discussions due to subsequent significant changes to the planned audit strategy and the reasons for such changes should be disclosed.

The audit committee's discussion and understanding of risks and critical audit issues

The audit committee should disclose how it has sought understanding of significant risks and critical audit issues. The committee should explain how such issues have been discussed with management and the external auditor. It should explicitly report on main audit issues raised by the external auditor and how the committee has reviewed any significant disagreements between the external auditor and management. Further, it should disclose initiatives taken to remedy any weaknesses, including actions related to risk and control systems.

The audit committee reporting should sufficiently explain how the committee has discussed and considered significant accounting policies and practices, the interpretation of relevant financial reporting standards, critical accounting estimates, and significant unusual transactions. It should be clear how the audit committee has assessed management's significant assumptions and justifications. The report should explain how the committee has ensured that management's approach to the valuation of assets and liabilities is robust and appropriate. The committee's discussions to the degree of aggressiveness or conservatism of the accounting and underlying estimates, as well as issues where management has had a wide room for judgement should be explained. Any use of independent experts to scrutinise the valuations and estimates by management should be disclosed.

Information of key personnel at the external audit

We believe better and more informative disclosure of how the audit committee evaluates the auditor, explicitly assessing the independence, experience, expertise and the extent of involvement of the audit partner and other key personnel assigned to the audit, is important. The auditor's objectivity and impartial and professional opinion is key to assuring investors of the accurateness of financial statements. There is however, an inherent conflict related to how auditors can perform an independent and objective audit, given that they are paid by the companies they audit.

⁵ Such communication would be in alignment with the requirements in the Public Company Accounting Oversight Board's accounting standard no 16: Communications with Audit Committees.



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We support that the names of the audit partner and other key personnel assigned to the audit are disclosed in the audit committee reporting, in addition to in the audit report itself. This will provide shareholders, in a timely manner, with the audit committee's assessment of the audit and the audit partner, available immediately upon filing of the annual report with the SEC.

As recognised in the concept release, the European Union has for more than eight years required that the audit partner sign the audit report⁶. Single jurisdictions, like the UK and Australia, also have similar requirements. In the US, the Federal Reserve already requires banks to provide names of their audit engagement partners.

Transparency requirements of audit partner and key audit personnel is supported by a growing body of empirical research indicating that such disclosure would enhance investor protection and provide useful information to investors⁷. The impact on audit quality is expected to be positive; it would encourage better audit procedures and supervision of the audit team, and more careful review of the audit results.

The audit partner's track record that would be compiled as the result of such disclosure requirements in the audit committee reporting will be key to the audit committee's evaluation of the external auditor, enhance investor protection, and provide useful information to investors. It will also be relevant to shareholders overseeing audit committees and determining whether to ratify the board's choice of outside auditor.

Once again, thank you for providing us with the opportunity to contribute our views. Should you have any questions or require any additional information about NBIM's views on this matter, please feel free to contact us.

Yours sincerely,

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William Ambrose
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⁶ Directive 2006/43 on Statutory Audits of Annual Accounts and Consolidated Account.

⁷ Joseph V. Carcello & Chan Li, *Costs and Benefits of Requiring an Engagement Partner Signature: Recent Experience in the United Kingdom*, 88 *Acct. Rev.* 1511, 1515 (2013) (" Our results are consistent with the argument that requiring an individual audit partner to sign a report improves audit quality by increasing the partner's accountability and transparency of audit reporting."),

