

## Corporate & Financial Weekly Digest

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### **Audits May Soon Require Even Greater Scrutiny of Executive Compensation**

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Citing a concern about increased risk of fraud and material misstatement, on February 28, the Public Company Accounting Oversight Board (the PCAOB) issued Release No. 2012-001 (the Proposal). The Proposal would amend public company auditing standards to require increased review and analysis of executive compensation programs because such programs can put pressure on management to meet financial performance targets to ensure larger compensation payments. The PCAOB believes that such pressure may result in a material misstatement of the company's financial position.

Existing standards already require the auditor to have a thorough understanding of the company's executive compensation programs. If adopted, the Proposal would amend Auditing Standard No. 12, Identifying and Assessing Risks of Material Misstatement, to require the auditor to undertake certain procedures to ensure that he or she has a thorough understanding of the company's executive compensation programs and whether the related performance metrics may increase the likelihood of misstated financial results to enlarge payments to executives. The Proposal would require the auditor to adopt specific procedures designed to identify risks of material misstatement. The Proposal provides that "such procedures should include, but are not limited to, (i) reading employment and compensation contracts and (ii) reading proxy statements and other relevant company filings with the Securities and Exchange Commission and other regulatory agencies that relate to the company's financial relationships and transactions with its executive officers."

The release of the Proposal is another in a long line of recent indicators that legislators, regulators and investors are still paying close attention to the amount and forms of compensation paid to executive officers, and the risk that intentional misstatements may occur to ensure that such compensation is increased. If the Proposal is adopted, public companies will want to work with their auditors to ensure that they have access to the required information so that audits can be completed in a timely and orderly fashion.

Public comment on the Proposal are invited and must be submitted to the PCAOB no later than May 15.

The Proposal can be found [here](#).

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