

# 2013 BDO BOARD SURVEY



**T**he responsibilities of corporate directors at publicly traded companies have never been greater. Dealing with regulatory changes to financial reporting requirements, addressing risk across the enterprise – whether it be in domestic operations, foreign markets or cyber space – and vigilantly managing executive compensation practices are a just a few of the issues that boards are wrestling with in 2013.

According to a new survey by the Corporate Governance Practice of BDO USA, LLP, most corporate directors believe regulatory and compliance overload is the greatest risk currently facing their business – far ahead of other threats, such as cyber breaches and corruption. Moreover, board members are resistant to proposed changes to the annual auditor's report and are beginning to monitor how the movement to link CEO compensation to equity may be creating a growing gap in compensation between chief executives and other members of management.

These are some of the findings of *The 2013 BDO Board Survey*, conducted by the Corporate Governance Practice of BDO USA, which examined the opinions of corporate directors of public company boards, with revenues ranging from \$250 million to \$750 million, regarding corporate governance issues. The survey, conducted in September 2013, covered various topics related to financial reporting, executive compensation, risk management and management of directors' time.

## BDO USA CORPORATE GOVERNANCE PRACTICE

BDO USA's Corporate Governance Practice is a valued business advisor to corporate boards. The firm works with a wide variety of clients, ranging from entrepreneurial businesses to multinational Fortune 500 corporations, on a myriad of accounting, tax, risk management and forensic investigation issues.

## CONTACT:

### WENDY HAMBLETON

312-616-4657 / [whambleton@bdo.com](mailto:whambleton@bdo.com)

### LEE GRAUL

312-616-4667 / [lgraul@bdo.com](mailto:lgraul@bdo.com)

### STEPHEN FERRARA

312-616-4683 / [sferrara@bdo.com](mailto:sferrara@bdo.com)

### ALBERT LOPEZ

305-420-8008 / [alopez@bdo.com](mailto:alopez@bdo.com)

### CHRISTOPHER TOWER

714-668-7320 / [ctower@bdo.com](mailto:ctower@bdo.com)

### MICHAEL WHITACRE

404-979-7116 / [mwhitacre@bdo.com](mailto:mwhitacre@bdo.com)

### ANDREW GIBSON

404-979-7106 / [agibson@bdo.com](mailto:agibson@bdo.com)

### RANDY RAMIREZ

212-885-8015 / [rramirez@bdo.com](mailto:rramirez@bdo.com)

### CARL PERGOLA

212-885-8575 / [cpergola@bdo.com](mailto:cpergola@bdo.com)

### GLENN POMERANTZ

212-885-8379 / [gpomerantz@bdo.com](mailto:gpomerantz@bdo.com)

▶ CONTINUED FROM PAGE 1

“Clearly, corporate board members aren’t sold on the usefulness of the PCAOB’s proposal to require external auditors to include more detailed information in the annual auditor’s report that accompanies a business’s financial statements. However, when you make changes to something that has been done the same way for more than 70 years, there is bound to be some pushback.”

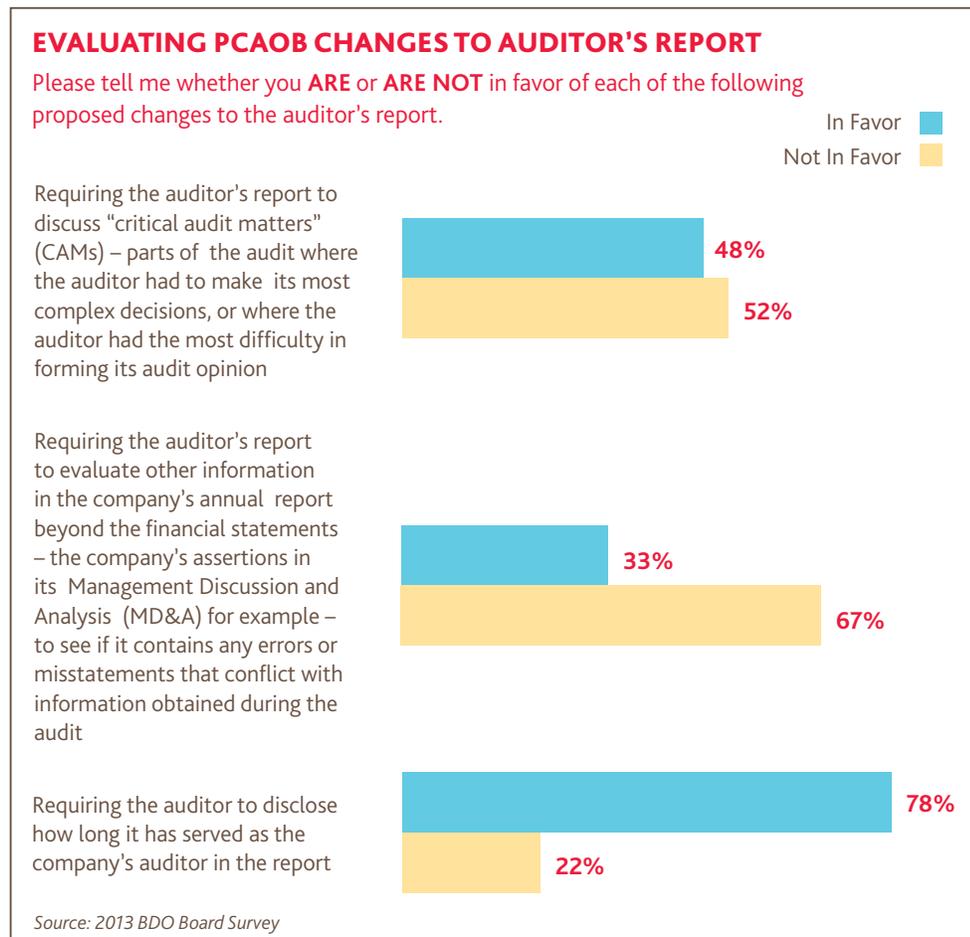
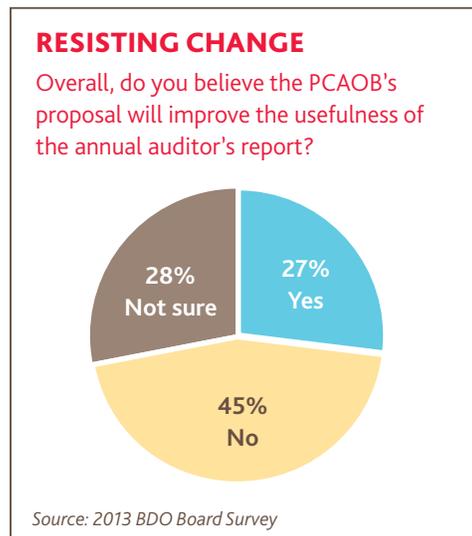
**Lee Graul, a Partner in the Corporate Governance Practice of BDO USA.**

▶ **FINANCIAL REPORTING**

In August of this year, the Public Company Accounting Oversight Board (PCAOB) issued a proposal to improve financial disclosure. The proposed changes will require external auditors to include more detailed information in the annual auditor’s report that accompanies a business’s financial statements. Yet, less than one-third (27%) of public company board members believe the PCAOB’s proposed changes will actually improve the usefulness of the report. Conversely, almost half (45%) of the directors say the changes will not improve the auditor’s report, while more than a quarter (28%) aren’t sure.

When asked about specific components of the PCAOB’s proposal, more than three-quarters (78%) of board members are in favor of the report disclosing the length of the external auditor’s tenure in the report. However, more than two-thirds (67%) of board members are opposed to the auditor’s report evaluating information beyond the financial statements for potential errors or misstatements that conflict with information obtained during the audit. A smaller majority (52%) is opposed to the report containing a discussion of critical audit matters that gave the auditor the most difficulty in forming its audit opinion.

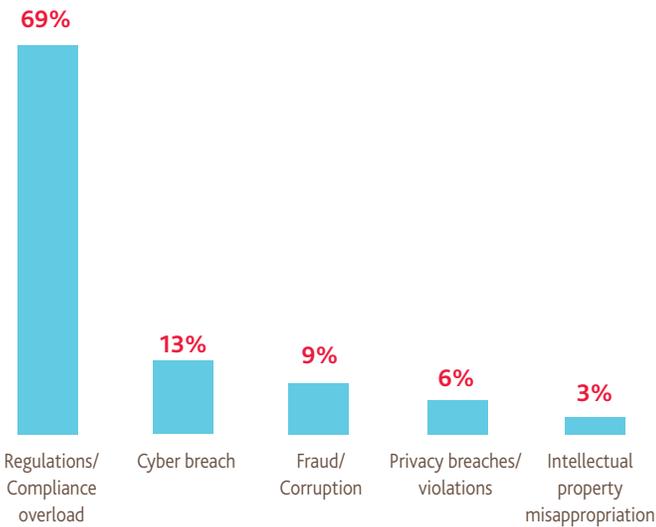
Close to two-thirds (64%) of corporate directors are aware of the new SEC rule that allows companies to disclose material information through postings on social media, but none indicate that their companies have utilized this new channel to do so and only 11 percent anticipate utilizing social media for material disclosures in the future.



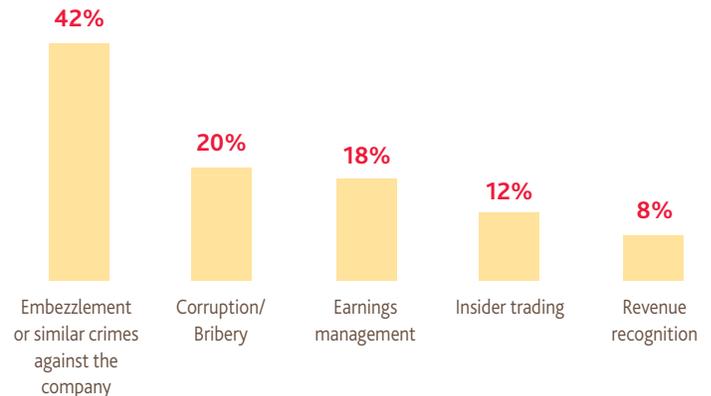
▶ CONTINUED FROM PAGE 2

**RANKING RISKS**

What issue represents the greatest risk for your business?



What area represents the greatest risk for FRAUD at your company?



Source: 2013 BDO Board Survey

**▶ RANKING RISKS**

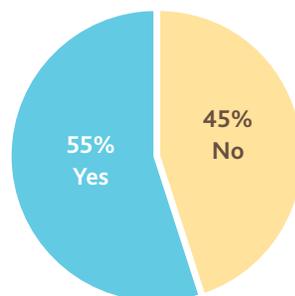
More than two-thirds (69%) of public company board members cite regulatory/ compliance overload as the greatest risk facing their businesses. Cyber breaches (13%), fraud/ corruption (9%), privacy violations (6%) and intellectual property misappropriation (3%) are cited by far smaller percentages of the directors.

When asked to identify the greatest risk for fraud at their companies, a large proportion of the directors cite embezzlement or similar crimes against the company (42%). Corruption/bribery (20%), earnings management (18%), insider trading (12%) and revenue recognition (8%) are cited by smaller proportions.

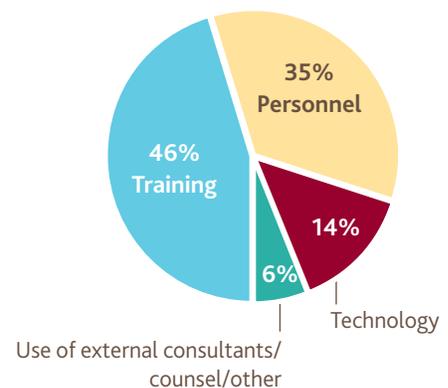
A majority (55%) of board members say they have increased their company's anti-fraud and anti-corruption resources in the past year. When asked where they have devoted the greatest percentage of those increased resources, almost half (46%) cite training and more than a third (35%) cite personnel. Smaller proportions cite technology (14%) and the use of external consultants (5%).

**CONFRONTING FRAUD**

Have you increased your company's anti-corruption and anti-fraud resources in the past year?



In which **ONE** of the following areas have you devoted the greatest increase in resources to reduce corruption and fraud?



Source: 2013 BDO Board Survey

"It is not surprising to see that companies are dealing with regulatory overload. The financial services sector, in particular, has been dealing with new regulations in both the U.S. and the EU. The directors' focus on training and education to improve compliance and reduce fraud is certainly positive news. Many of the companies we work with perform a comprehensive risk assessment addressing fraud and corruption. The risk assessment results often guide the company towards additional and more strategic training and education. By proactively conducting independent risk assessments, businesses can greatly enhance their risk mitigation efforts."

**Glenn Pomerantz, Partner in Charge of Global Forensics at BDO Consulting**

▶ CONTINUED FROM PAGE 3

### ▶ CYBER RISK

Just 11 percent of board members say their company has experienced a cyber breach during the past two years. Nevertheless, cyber security has been a regular topic in the media and corporate directors appear to be paying attention.

Close to half (47%) of directors say they have completed documenting all of the critical cyber assets of their company and a similar percentage (45%) say they are currently in the process of identifying their critical cyber assets. Just 9 percent indicate they have taken no steps to identify these critical assets.

When asked about specific steps their businesses have taken to mitigate cyber security risks, almost all (98%) of the board members indicate they have implemented technology to safeguard the company. Approximately half of the directors say they hired cyber security consultants to either advise on risk areas (56%) or supplement IT procedures (49%). A similar percentage (48%) indicate they formed a risk committee to create cyber policies/procedures. Just 18% say they have purchased cyber insurance to cover potential losses from cyber crime.

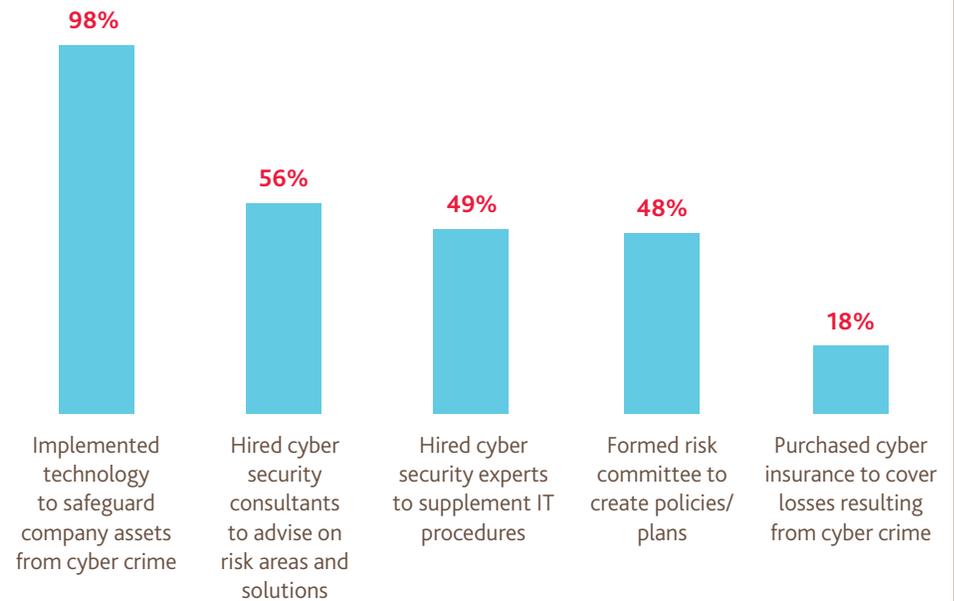
### ▶ FOREIGN MARKET RISK

A majority (56%) of the directors say their company conducts business in foreign locations or with foreign customers or suppliers. Of those conducting business internationally, a majority (55%) indicate that they deal with foreign government officials and better than one-third (38%) of those believe compliance risks related to bribery of foreign officials have increased over the past two years, compared to just 10 percent reporting a decrease.

When asked to identify what is the most effective tool businesses can use to mitigate corruption risks in foreign markets, almost two-thirds (65%) of the directors cite improved training and education of employees. Increased testing of transactions (16%), expanded board oversight (8%), a change in business model (8%) and revamped policies and procedures (8%) are other measures cited by the directors.

### MANAGING CYBER SECURITY

What public companies are doing to mitigate cyber security risks:



Source: 2013 BDO Board Survey



▶ CONTINUED FROM PAGE 4

“The concern with the gap in compensation between the CEO and other members of management is a subject we are increasingly being asked to address by clients. Given the ongoing increase in equity markets and the SEC’s current proposal to require companies to disclose the ratio of CEO pay to median employee pay, this issue is only going to get bigger. Boards must decide whether they want to close the gap by expanding equity pay to other members of management, moving more CEO compensation back to traditional compensation or a combination of both of these strategies.”

**Randy Ramirez, a Senior Director on Compensation in the Corporate Governance Practice of BDO USA**

## ▶ EXECUTIVE COMPENSATION

In recent years, CEO compensation has become increasingly tied to equity in order to link pay to performance and align CEOs with shareholders. However, given the sensational performance of the stock market in 2013, one-third (34%) of public company board members are concerned that this focus on equity is leading to a growing gap in compensation between the CEO and other members of the management team.

Of those expressing this concern, a majority (56%) believe the most appropriate approach to address the gap is to expand equity-based compensation to more members of the management team, while one-third (33%) suggest moving a larger portion of CEO compensation back to traditional, long-term cash or annual cash incentive programs. Few (11%) suggest re-introducing executive perquisites back into the compensation mix for key employees.

When asked what performance measurement they consider the best substitute for at least a portion of equity-linked pay, board members cite profit growth (39%) and free cash flow (24%) as the most likely substitutes. Operational efficiency (18%), revenue growth (14%) and market share (6%) are the other alternative measurements cited by the directors.

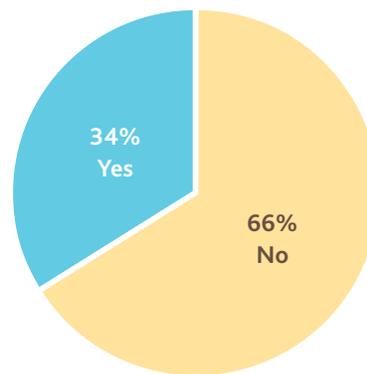
In a related area, the vast majority (82%) of board members at public companies believe proxy advisory firms should be subject to SEC oversight due to the potential for a conflict of interest in providing services to both corporations and institutional shareholders.

## ▶ BOARD PRIORITIES

When asked what topics they would like to spend more or less of their time on, close to half of the board members cite succession planning (47%) and studying industry

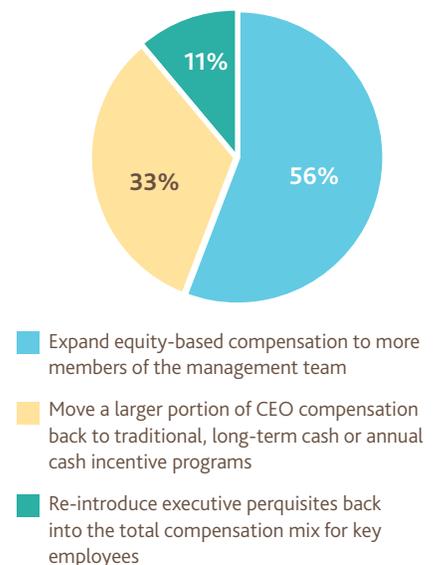
### EXECUTIVE PAY GAP

Given the sensational performance of the stock market in 2013, are you concerned that the focus on equity in CEO compensation is leading to a growing gap in compensation between the CEO and other members of management?



Source: 2013 BDO Board Survey

What do you consider the most effective step to address the growing gap in pay between CEOs and other members of the management team?



### TIME MANAGEMENT

Would you like your board to spend more or less time on each of the following topics?

Topic	More	Less	Same
Succession planning	47%	5%	47%
Industry competitors	45%	5%	50%
Risk management	38%	1%	61%
Evaluating management performance	32%	-----	68%
Compliance and regulatory issues	16%	20%	64%
Executive compensation	8%	8%	84%

Source: 2013 BDO Board Survey

competitors (45%) as areas where they would like to spend more time. Risk management (38%) and evaluating management performance (32%) were the other areas where sizable percentages expressed an

interest in spending more time. Perhaps more revealing is how few of these directors expressed a desire to spend less time on any of these areas, with the possible exception of compliance and regulatory issues.



#### **ABOUT THE SURVEY**

These are the findings of *The 2013 BDO Board Survey* which examines the opinions of 74 corporate directors of public company boards, with revenues ranging from \$250 million to \$750 million, regarding financial reporting and corporate governance issues. The survey was conducted in September of 2013.

#### **ABOUT BDO USA**

BDO is the brand name for BDO USA, LLP, a U.S. professional services firm providing assurance, tax, financial advisory and consulting services to a wide range of publicly traded and privately held companies. For more than 100 years, BDO has provided quality service through the active involvement of experienced and committed professionals. The firm serves clients through 49 offices and more than 400 independent alliance firm locations nationwide. As an independent Member Firm of BDO International Limited, BDO serves multinational clients through a global network of 1,118 offices in 135 countries.

BDO USA, LLP, a Delaware limited liability partnership, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms. BDO is the brand name for the BDO network and for each of the BDO Member Firms. For more information, please visit: [www.bdo.com](http://www.bdo.com).

Material discussed is meant to provide general information and should not be acted on without professional advice tailored to your firm's individual needs.