NATIONAL DIRECTORS INSTITUTE | NDI Executive Exchange

Top Takeaways

Audi Committee Roundtable – PCAOB Gone Wild

These are the top takeaways from the **Audit Committee Roundtable – PCAOB Gone Wild** moderated by Foley Partner Mark Plichta on November 17, 2011 as part of the NDI Executive Exchange, a segment of Foley's National Directors Institute. Featured participants in the roundtable were Ken Best of Fiserv, Inc.; Patrick (P.J.) DiStefano from Deloitte & Touche LLP; Isaac Kaufman of Advanced Medical Management; and Aldo Pagliari from Snap-On, Incorporated.

1. The U.S. Public Company Accounting Oversight Board (PCAOB) has issued a concept release regarding expansion of auditor reports, including:
   - Inclusion of an Auditor's Discussion and Analysis (AD&A) section;
   - Required and expanded use of "emphasis of matter" paragraphs in the auditor's report;
   - Reporting on information outside the financial statements; and
   - Clarification of certain language in the auditor's report.
2. The PCAOB also issued a concept release regarding auditor independence, including mandatory audit firm rotation after a certain number of years. The PCAOB's objective is to enhance auditor objectivity, independence and professional skepticism.
3. Panel participants were not in favor of requiring auditors to include an AD&A section in their reports as proposed by the PCAOB.
   - If auditors are required to opine on information in their own independent AD&A, there is a risk that management may not be as forthcoming with information given to the auditors, resulting in less effective audits.
   - The AD&A also presents a risk of producing "dueling discussions" between the AD&A (produced by the auditors) and MD&A (produced by management). This conflict might confuse investors reading the information, contrary to the purpose of providing such reports in the first place.
   - Comparability is a standard quality found in traditional auditor's reports. The AD&A, given the nature of the disclosures proposed by the PCAOB, may lack this comparability and thus be less effective than traditional reports.
   - If auditors are required to complete an AD&A, the report may quickly be reduced to boilerplate language, thus reducing any positive impact that it might have.
   - Contrary to the general disapproval of the AD&A, some believe that investors may benefit from additional information, such as the auditors' views on use of estimates or similar judgments.
   - Overall, the consensus was that the AD&A has very little "value add" to companies, their shareholders or other stakeholders.
4. Several members of the group felt that information that might be included in expanded emphasis paragraphs is best disclosed by the company instead of the auditors. Furthermore, much of that information is already included in the footnotes and MD&A. As a result, there was little support for expanded emphasis paragraphs.

5. Auditors already review earnings releases and typically the MD&A in the course of their audit work, and management has an acceptable level of comfort with such reviews. However, additional requirements would likely require additional procedures and cost and may impact timing.

6. The group supported adding clarifying language to the standard auditor's report, as such language would add clarity, reduce litigation risk and not create any significant new costs.

7. The increased costs associated with the loss of firm and individual auditor knowledge that would be caused by mandatory audit firm rotation outweigh any real benefits of such rotation. Fees would increase to cover the learning curve of a new auditor.

8. The pool of large, international, and sophisticated firms is small, limiting any company's auditor options, especially considering the existing independence rules prohibiting auditors from providing non-audit services to audit clients. Many companies that use a Big Four auditor also use two Big Four firms for non-audit services, so they would have only one independent firm to "choose" from among Big Four firms whenever they would be forced to rotate firms.

9. The general view of participants was that audit partners and firms are already independent and not tied to management, so there is no need for firm rotation or other new independence rules.

10. Someone would have to pay for all of this. The primary intended beneficiaries of the proposals – the shareholders of public companies – will ultimately end up paying the costs of these proposals.

For more information
For more information on the Audit Committee Roundtable – PCAOB Gone Wild session, please feel free to contact the moderator directly:

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