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Report from the Working Group on Auditor Interaction with Audit Committees

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Audit Committee Expertise

Financial Expert Requirements:

- ❑ an understanding of financial statements and generally accepted accounting principles;
- ❑ an ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;
- ❑ experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, OR experience actively supervising one or more persons engaged in such activities;
- ❑ an understanding of internal controls and procedures for financial reporting; and
- ❑ an understanding of audit committee functions.

Audit Committee Expertise

Financial Expert Background:

- ❑ Experience as principal financial officer, OR principal accounting officer, OR controller, OR public accountant OR auditor OR experience with similar functions; OR
- ❑ Experience as supervisor of persons performing above functions; OR
- ❑ Experience overseeing OR assessing the performance of companies OR public accountants with respect to the preparation, OR auditing OR evaluation of financial statements; OR
- ❑ Other relevant experience (not defined). Company must briefly describe.

AS 16 - Auditor Communications with Audit Committee

AS 16:

- ❑ Issued August 5, 2012
- ❑ Effective for audits of most issuers beginning on or after Dec. 15, 2012
- ❑ Increased outreach by PCAOB to directors and audit committee members

AS 16

Auditor must:

- ❑ Provide timely communications
- ❑ Document communications
- ❑ Establish understanding of terms of audit engagement
- ❑ Inquire whether audit committee is aware of matters relevant to audit
- ❑ Communicate overall audit strategy, any significant changes

Auditor must communicate:

- ❑ Significant and critical accounting policies and practices
- ❑ Critical accounting estimates
- ❑ Significant unusual transactions
- ❑ Evaluation of quality of company's financial reporting
- ❑ Going concern issues
- ❑ Uncorrected and corrected misstatements
- ❑ Difficult or contentious matters for which auditor was consulted
- ❑ Management consultation with other accountants
- ❑ Material written communications
- ❑ Disagreements with management
- ❑ Difficulties encountered in performing the audit

AS 16

Questions:

- ❑ Should AS 16 be amended to require auditors to provide the Part 1 (public) findings of their most recent inspection report, along with a summary of Part 2 (non-public) findings?
- ❑ Does AS 16 miss other important auditor-to-audit committee communications?

Audit Committee Communications to Investors

Audit Committee must disclose:

- ❑ Committee member information (independence, financial expert, service on other audit committees)
- ❑ Statement whether mandatory matters were discussed with auditor (auditor's responsibilities, audit strategy and timing, significant issues)
- ❑ Statement whether mandatory information from auditor was received regarding independence and whether discussed
- ❑ Pre-approval policies and procedures for audit and non-audit services
- ❑ Two-years aggregate fees (audit, audit-related, tax, other)
- ❑ Charter:
 - Purpose
 - Responsibility for appointment, compensation and oversight of auditor
 - Statement on annual performance evaluations of Committee
 - Duties of Committee, including reviewing auditor report

Audit Committee Communications to Investors

What should audit committees report to shareholders?



Require audit committees to provide information

What information should shareholders receive?



Require auditors to provide information



Require auditors to provide information unless provided by audit committee.

Audit Committee Communications to Investors

Most Common Voluntary Audit Committee Disclosures

- Consideration of non-audit fees (67%)
- Non-audit services provided and why appropriate (NA)
- Disclosure of auditor tenure (32%)
- Oversight of auditor beyond required information (32%)
- Factors considered in evaluation/retention of auditor (15%)

Audit Committee Communications to Investors

Shareholder Proposals Requesting Audit Committee Disclosure

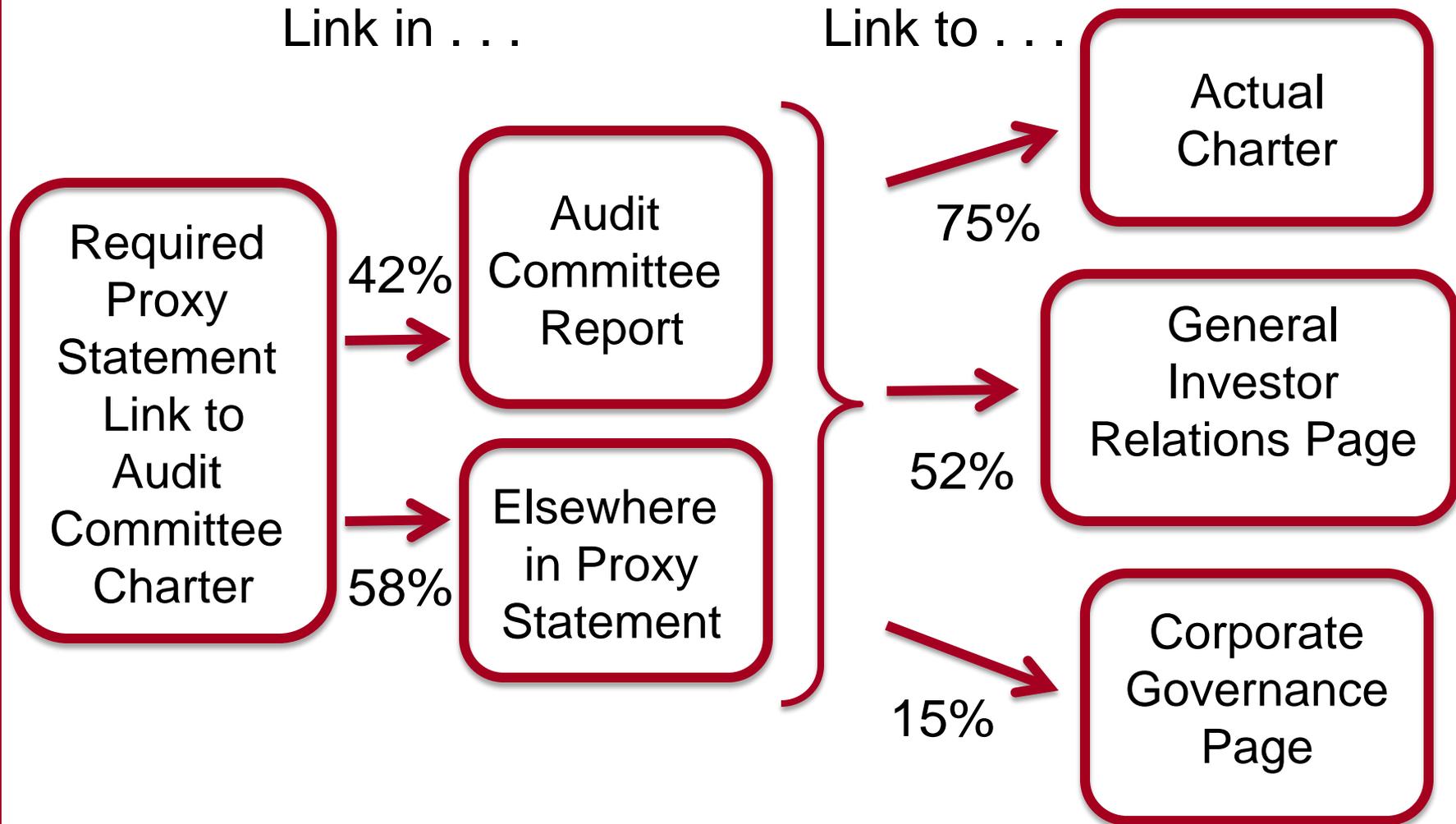
Excludable as ordinary business operations

- ❑ Auditor tenure
- ❑ Aggregate fees paid
- ❑ Policy/Practice of considering rotation or seeking competitive bids
- ❑ Mandated practice of lead audit partner rotation
- ❑ Assessment of auditor tenure risks
- ❑ Training programs for Committee on auditor independence
- ❑ Any additional policies related to auditor independence

Audit Committee Communications to Investors

Voluntary Audit Committee Disclosure	Audit Committee Report	Proxy Statement
Consideration of non-audit fees (67%)	52%	15%
Non-audit services provided and why appropriate (NA)	25%	75%
Oversight of auditor beyond required information (32%)	28%	4%
Disclosure of auditor tenure (32%)	1%	31%
Factors considered in evaluation/retention of auditor (15%)	6%	9%

Audit Committee Communications to Investors



Audit Committee Communications to Investors

Audit Committee Public Disclosures: Sampling of Recommendations

- ❑ UK Competition Commission: Report to shareholders on findings of AQR reports; state grade awarded and how committee and auditor are responding
- ❑ The UK Corporate Governance Code: If auditor provides non-audit services, explain how auditor objectivity and independence is safeguarded
- ❑ Council of Institutional Investors: Explain why an auditor with more than 10 year tenure was renewed
- ❑ Canadian Public Accountability Board CPAs: Conduct a comprehensive review of auditor at least every five years resulting in a recommendation to retain or replace and report publicly on the scope and process

Audit Committee Communications to Investors

Sources

Statutory Audit Services Market Investigation: Summary of Provisional Decision on Remedies, UK Competition Commission (July 22, 2013)

The UK Corporate Governance Code, Financial Reporting Council (Sep. 2012)

Corporate Governance Policies, Council of Institutional Investors

Enhancing Audit Quality: Conclusions and Recommendations, Canadian Public Accountability Board and Chartered Professional Accountants Canada (May 2013)

Audit Committee Reporting to Shareholders: 2013 Proxy Season Update, Ernst & Young (2013)

Audit Committee Reporting to Shareholders: Going Beyond the Minimum, Ernst & Young (Feb. 2013)