

NOTICE: This is an unofficial transcript of the portion of the Public Company Accounting Oversight Board's Standing Advisory Group meeting on December 1, 2016 that relates to *Proposed Amendments Relating To The Supervision of Audits Involving Other Auditors And Proposed Auditing Standard—Dividing Responsibility for the Audit With Another Accounting Firm*. The other topics discussed during the November 30-December 1, 2016 meeting are not included in this transcript excerpt. The Public Company Accounting Oversight Board does not certify the accuracy of this unofficial transcript, which may contain typographical or other errors or omissions. An archive of the webcast of the entire meeting can be found on the Public Company Accounting Oversight Board's website at: <https://pcaobus.org/News/Events/Pages/SAG-meeting-November-2016.aspx>.

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

(202) 234-4433

www.nealrgross.com

PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

+ + + + +

STANDING ADVISORY GROUP

+ + + + +

MEETING

+ + + + +

THURSDAY,
DECEMBER 1, 2016

+ + + + +

The Advisory Group convened in Academy Hall in the headquarters of FHI 360, located at 1825 Connecticut Avenue, NW, Washington, DC, at 8:30 a.m., Marty Baumann, Moderator, presiding.

PRESENT:

JOAN C. AMBLE, President, JCA Consulting, LLC
 PRAT BHATT, Senior Vice President, Corporate
 Controller and Chief Accounting Officer, Cisco
 Systems, Inc.
 PETER C. CLAPMAN, Senior Advisor, CamberView
 Partners, LLC
 CHARLES M. ELSON, Edgar S. Woolard, Jr. Chair of
 Corporate Governance and Director, John L.
 Weinberg Center for Corporate Governance,
 University of Delaware
 MICHAEL J. GALLAGHER, Managing Partner, Assurance
 Quality, PwC
 SYDNEY K. GARMONG, Partner in Charge, Regulatory
 Competency Center, Crowe Horwath, LLP
 KENNETH A. GOLDMAN, Chief Financial Officer, Yahoo, Inc.
 L. JANE HAMBLEN, Former Chief Legal Counsel, State of
 Wisconsin Investment Board
 ROBERT B. HIRTH, JR., Chairman, Committee of

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
 1323 RHODE ISLAND AVE., N.W.
 WASHINGTON, D.C. 20005-3701

Sponsoring Organizations of the Treadway
Commission

PHILIP R. JOHNSON, Former Nonexecutive Director,
Yorkshire Building Society

JEAN M. JOY, Director of Professional Practice and
Director of Financial Institutions Practice, Wolf
& Company, PC

GUY R. JUBB, Former Global Head of Governance and
Stewardship, Standard Life Investments, Ltd.

DAVID A. KANE, Americas Vice Chair, Assurance
Professional Practice, Ernst & Young, LLP

SARA GROOTWASSINK LEWIS, Chief Executive Officer, Lewis
Corporate Advisors, LLC

JON LUKOMNIK, Executive Director, Investor Responsibility
Research Center Institute; Managing Partner,
Sinclair Capital, LLC

DOUGLAS L. MAINE, Limited Partner and Senior Advisor,
Brown Brothers Harriman & Co.

MAUREEN McNICHOLS, Marriner S. Eccles Professor of
Public and Private Management and Professor of
Accounting, Stanford University

DAVID J. MIDDENDORF, National Managing Partner-Audit
Quality & Professional Practice, KPMG LLP

RICHARD H. MURRAY, Chief Executive Officer, Liability
Dynamics Consulting, LLC

KAREN K. NELSON, M.J. Neeley Professor of Accounting,
Texas Christian University

ZACH OLEKSIUK, Americas Head, Corporate Governance and
Responsible Investment, BlackRock

GREGORY A. PRATT, Chairman, President and Chief
Executive Officer, Carpenter Technology
Corporation

SRIDHAR RAMAMOORTI, Associate Professor of Accounting,
School of Accountancy and Director, Corporate
Governance Center, Kennesaw State University

BRANDON J. REES, Deputy Director, Office of Investment,
AFL-CIO

PHILIP J. SANTARELLI, Partner, Baker Tilly Virchow
Krause, LLP

THOMAS I. SELLING, President, Grove Technologies, LLC

CHARLES V. SENATORE, Executive Vice President, Head of
Regulatory Coordination and Strategy, Fidelity
Investments

DAVID M. SULLIVAN, National Managing Partner - Quality
& Professional Practice, Deloitte & Touche, LLP

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

SIR DAVID P. TWEEDIE, Chairman, International
Valuation Standards Council
CULLEN WALSH, on behalf of Larry Smith of the FASB
JOHN W. WHITE, Partner, Corporate Department,
Cravath, Swaine & Moore, LLP
MEGAN ZIETSMAN, on behalf of Arnold Schilder of the IAASB

PCAOB BOARD MEMBERS:

JEANETTE FRANZEL
JAY HANSON
STEVEN HARRIS

OBSERVERS PRESENT:

JIM DALKIN, GAO
ANN DUGUID, FINRA
HARRISON GREENE, FDIC
MARC PANUCCI, SEC
MIKE SANTAY, Grant Thornton
CULLEN WALSH, FASB

PCAOB STAFF:

DIMA ANDRIYENKO, Associate Chief Auditor
MARTIN F. BAUMANN, Chief Auditor and Director of
Professional Standards
JAMES R. DOTY, Chairman
STEPHANIE HUNTER, Assistant Chief Auditor
DENISE MUSCHETT WRAY, Assistant Chief Auditor
JESSICA WATTS, Associate Chief Auditor
KEITH WILSON, Deputy Chief Auditor

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 MR. ANDRIYENKO: Thank you, Marty. We are happy
2 to give you an overview of comments on the proposal on the
3 supervision of other auditors. I am going to go through
4 a few introductory slides and I am going to turn it over
5 to my colleagues after that.

6 Joining me for the presentation today are Denise
7 Muschett Wray and Stephanie Hunter to my right. They have
8 put a lot of effort in preparing the proposal. Now we have
9 been all working hard together analyzing comments in the
10 comment letters. Also at the table is Deputy Chief
11 Auditor Keith Wilson, who also works on the proposal.

12 I am going to put the slide up. I am not going to
13 go through the standard disclaimer. I just wanted to
14 note, perhaps stating the obvious, that our presentation
15 is a fairly high-level overview of comments. The actual
16 comment letters in their entirety are, of course, on our
17 website in Rulemaking Docket 42.

18 This slide is a very brief refresher on the project.
19 The proposal was issued on April 12th this year. It was
20 designed to increase the lead auditor's involvement in an
21 evaluation of the work of other auditors, also to enhance
22 the lead auditor's ability to either prevent or detect

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 deficiencies in the work of other auditors, and
2 ultimately, to facilitate improvements in the quality of
3 work of other auditors.

4 The proposal builds on the existing requirements
5 in PCAOB standards. It would amend several of the
6 existing standards, namely standards of supervision,
7 planning, the engagement of quality review, and
8 documentation. It would supersede one of the existing
9 PCAOB standards, the one that has been on the books since
10 the early 1970s and currently governs some of the audits
11 that involve other auditors, that is AS 1205 or, as we
12 currently know it, AU 543.

13 And finally, the proposal would provide a new
14 auditing standard for situations in which the lead auditor
15 divides the responsibility for the audit with another
16 accounting firm. So, this is a proposed standard 1206.
17 And currently, these audits are governed by AS 1205.

18 On this slide, you can see who actually commented
19 on the proposal. The PCAOB received 23 comment letters,
20 most of which came from the accounting profession, the
21 accounting firms and associations of accountants.

22 The proposal included almost 60 fairly detailed

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 questions to commenters and we did receive some very
2 detailed responses to our questions. Many of the
3 commenters responded to either every single question or
4 covered all of the key areas of the proposal. And we are
5 currently going through the comments. We are analyzing
6 the comments. Our discussions are still ongoing within
7 the team and within the PCAOB.

8 Just a few words about general themes in comments.
9 In general, commenters agreed with the stated reasons in
10 the proposal for amending auditing standards and also with
11 the general direction that the proposal took, which is to
12 require that the lead auditor uses risk-based approach to
13 supervising other auditors. And that is important for
14 determining the appropriate extent of supervision of the
15 other auditor, appropriate extent of involvement in the
16 work of other auditors and evaluation of their work.

17 And you can see on the slide the commenters said
18 that -- some commenters said that many of the proposed
19 changes are a step in the right direction, that it would
20 improve the quality of audits, and enhance investor
21 protection. But there are comments that indicated
22 concern whether the proposal really strikes the right

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 balance between the lead auditor's involvement in the
2 audit and the other auditor's involvement in the audit.
3 And even those who supported the overall direction of the
4 proposal were asking questions and asking for
5 clarification on certain aspects of the proposal and then
6 making suggestions in their comment letters. And we are
7 going to go through those comments, as we go through the
8 presentation.

9 These are the key areas of comment that we thought
10 we would cover today. We would start, naturally, with
11 audit planning, which includes several proposed
12 requirements, including the sufficiency of ---
13 requirements for determining sufficiency of the lead
14 auditor's participation in the audit, requirements
15 related to determining compliance of --- the other
16 auditor's compliance with ethics and independence,
17 requirements of the PCAOB and the SEC, and the assessment
18 of the knowledge, skill, and abilities of the other
19 auditor.

20 Then, we will move on to comments related to
21 supervisory requirements in the proposal. We will talk
22 about the divided responsibility audits, that is the new

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 proposed standard, and the requirements for the engagement
2 quality review.

3 Then, we will talk about a potential unintended
4 consequence of the proposal, whereas, the other auditor
5 may feel a little less accountable for their work, now that
6 the lead auditor is going to be more involved in the audit.

7 And we will conclude with discussing comments and
8 various aspects of the economic analysis.

9 I am going to turn the mike over to Denise. She
10 will cover the area of planning and she will talk about
11 some of the supervisory requirements. And then Stephanie
12 will continue on. She will wrap up the supervision and
13 cover the rest of the topics.

14 MR. BAUMANN: And I just wanted to point out some
15 may not be clear in the slides up there on the screen.
16 Everybody should have a copy of these slides in their
17 folder.

18 MS. WRAY: Thank you, Dima. Good morning,
19 everyone. As Dima indicated, I will go over with you
20 comments we received on the proposed requirements related
21 to planning an audit that involves the use of other
22 auditors. So, it is proposed amendments to AS 2101 as well

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 as comments we received on a couple of the proposed
2 requirements related to supervision of the work of the
3 other auditor.

4 And so on this first slide, we have summarized
5 comments we received relating to a proposed requirement
6 that the engagement partner determines whether his or her
7 firm is sufficiently involved in the audit to serve as lead
8 auditor. The determination would be based on the risk of
9 material misstatement associated with the portion of the
10 financial statement audited by the engagement partner's
11 firm relative to the portion audited by the other auditors.

12 Ordinarily, the lead auditor would need to audit
13 the location at which the primary financial reporting
14 decisions were made and the consolidated financial
15 statements were prepared in order to address the risk
16 related to these very important judgments and activities.
17 As well, the auditor would need to audit a sufficient
18 number of other locations to cover the greater portion of
19 risk than any other audit firm that is involved in the
20 audit.

21 As we can see on the slide, some commenters
22 indicated that an auditor should not issue an opinion when

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 not sufficiently involved in an audit and that describing
2 the sufficiency criteria in the standard, in terms of risk,
3 is appropriate.

4 Several commenters were concerned whether the
5 proposed requirements could be effectively applied to
6 certain situations they encountered in practice. Some of
7 these commenters asked the Board to provide more examples
8 in the release to illustrate how these scenarios would be
9 addressed by the amendments. For example, some
10 commenters asked to clarify how the proposed requirements
11 would apply when one auditor audits a significant portion
12 or a sizeable portion of the company or when more than one
13 auditor audits a sizeable portion of the company.

14 A few commenters asked us to clarify whether the
15 lead auditor's close supervision of another auditor could
16 be counted towards the lead auditor's participation in the
17 audit.

18 Several commenters asked questions about
19 situations in which the auditor who meets the sufficiency
20 criteria is not licensed in the jurisdiction of the
21 issuer's headquarters. For example, if the issuer is
22 headquartered in a U.S. state that requires the auditor

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 to be licensed in that state, commenters asked the Board
2 to provide more explanation about how the requirements
3 would be implemented in those situations.

4 The second comment theme relating to audit planning
5 addresses the proposed requirement for the lead auditor
6 to determine the other auditor's compliance with ethics
7 and independence requirements of the PCAOB and the SEC.
8 The proposal would require the lead auditor to gain an
9 understanding of the other auditor's knowledge of and
10 experience in applying the ethics and independence
11 requirements and obtain a written representation of
12 compliance from the other auditors.

13 The proposed requirement is intended to provide the
14 lead auditor with specific direction for complying with
15 existing requirements for planning an audit that involves
16 other auditors. Several commenters supported obtaining
17 from other auditors a written representation of compliance
18 with ethics and independence requirements.

19 We do note, however, that some commenters observed
20 that when read in conjunction with the proposed definition
21 of other auditor, the use of other auditor in this
22 particular requirement could be interpreted to mean that

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 the lead auditor would need to obtain a written
2 representation from each individual engagement team
3 member who is not employed with the lead auditor.

4 Several commenters also recommended clarifying
5 whether the lead auditor can rely on the quality control
6 system of another auditor from the same audit network when
7 determining which procedure the lead auditor should
8 perform to comply with the proposed amendments.

9 This slide shows the last set of comments on the
10 proposed requirements related to planning that we will
11 discuss and it relates to those requirements for the lead
12 auditor's understanding of the knowledge, skill, and
13 ability of certain engagement team members at the other
14 auditor.

15 Commenters generally agreed that understanding the
16 qualifications of the other auditor is important when the
17 lead auditor determines the extent of its supervision of
18 the work of other auditors. However, this is also an area
19 for which commenters wanted to know if the lead auditor
20 may rely on its network's quality control system when the
21 other auditor and the lead auditor are in a common network.

22 For this particular requirement, commenters

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 thought that the lead auditor should be able to rely on,
2 for example, information regarding their network's
3 training policies and programs.

4 Some commenters thought that the proposed
5 requirement should apply only to those engagement team
6 members at the other auditor who assists the engagement
7 partner with planning and supervision. Other commenters
8 thought the requirement should be expanded to apply to
9 other engagement team members of the other auditors.

10 Commenters who were in favor of expanding the
11 requirement were concerned, for example, that, as
12 proposed, the requirement does not contemplate those
13 engagement team members of the other auditor's firm who,
14 although not assisting the engagement partner with
15 planning and supervision, perform work that is significant
16 to the audit.

17 Specialists who are part of other auditor's team
18 and perform work that is significant to the audit as a whole
19 were cited as an example of where expansion of this
20 requirement could, in the views of those commenting, lead
21 to improvement in audit quality.

22 One commenter suggested that the Board consider

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 allowing the lead auditor to determine on a case-by-case
2 basis whether to apply this requirement only to those
3 engagement team members assisting with planning and
4 supervision or to other engagement team members on the
5 other auditor's team.

6 With this slide, I will now switch gears to the
7 proposed requirements related to supervising the other
8 auditor's work. Before jumping into the actual themes,
9 it may be worth repeating that the proposed requirements
10 are intended to build on existing supervision requirements
11 that are in our standards for the work of other auditors
12 and it is intended to give the lead auditor more specific
13 directions in terms of how to comply with existing
14 standards, existing requirements.

15 With that, the first comment theme that we have on
16 this slide relates to the proposed requirement for the lead
17 auditor to inform the other auditors in writing about their
18 responsibilities. Some commenters were generally in
19 agreement that written communication of the lead auditor's
20 instructions to other auditors would improve audit
21 quality.

22 Some commenters were unclear as to whether the lead

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 auditor's communication should include all the risks or
2 only those relevant to the other auditor's work. The
3 commenters who had this concern indicated that requiring
4 the lead auditor to communicate all risks would be too
5 broad of a requirement and could result in significantly
6 more work.

7 The second half of the slide deals with comments
8 on a proposed requirement for the lead auditor to obtain
9 from other auditors a written report that would describe
10 the other auditor's procedures, findings, conclusion, and
11 where applicable, opinion.

12 We noted that the intended scope of this particular
13 communication appeared to be unclear for some commenters.
14 Some commenters, for example, discussed scaling this
15 requirement to the scope of the other auditor's work. One
16 commenter noted that for certain circumstances, the Board
17 could consider allowing the lead auditor to conduct
18 discussions with the other auditor and perform a more
19 detailed review of the other auditor's work as an
20 alternative to this written report.

21 Other commenters asked whether the Board intends
22 for the other auditor to report to the lead auditor a

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 summary of each procedure performed by the other auditor
2 or provide a more risk-based reporting of procedures
3 performed to address high-risk areas. Some of those who
4 commented on this requirement asked for additional
5 guidance on the form and content of this written report.

6 This slide has the last area that I will cover for
7 you and it relates to the proposed requirement for the lead
8 auditor to review a description of other auditors' planned
9 audit procedures and the results of the other auditor's
10 work.

11 Some commenters noted a few areas in which these
12 proposed requirements could be clarified. For example,
13 some commenters noted that a requirement for the lead
14 auditor to review detailed audit programs of the other
15 auditor would be too onerous, especially when the other
16 auditor is performing a full-scope audit.

17 Some commenters asked that the Board consider
18 allowing the lead auditor to better leverage the review
19 performed by partners and managers of the other auditor's
20 firm who are experienced and well-qualified. One
21 commenter asked that the Board clarify the application of
22 the review requirement in certain circumstances, such as

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 when the lead auditor uses a translator for work that has
2 been documented in a foreign language.

3 Lastly, several commenters ask whether the lead
4 auditor may leverage its network quality control system
5 -- again, as you can see, this is a common question -- in
6 determining the extent to which it performs these
7 requirements for other auditors within the lead auditor's
8 network.

9 I will now turn it over to Stephanie to complete
10 the other supervision comments in the other areas.

11 MS. HUNTER: Thank you, Denise.

12 Okay, so I will cover the final comment theme
13 relating to the lead auditor's supervision of other
14 auditors. And specifically, I am going to discuss the
15 comments on the supervisory requirements for multi-tiered
16 audits.

17 To review the proposal, in an audit involving
18 multiple tiers of other auditors, the proposal would allow
19 the lead auditor to direct the first other auditor to
20 perform, on behalf of the lead auditor, certain
21 supervisory procedures with respect to the second other
22 auditor.

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 Certain other supervisory procedures should be
2 performed by the lead auditor, such as communicating scope
3 of work, tolerable misstatement and risk of material
4 misstatement.

5 As you can see on the slide, commenters generally
6 view the involvement of first-tier other auditors in
7 supervising lower-tier other auditors as important
8 because of the first-tier other auditor's knowledge of
9 company business at their level.

10 Some commenters suggested allowing for greater
11 involvement of first-tier other auditors and supervising
12 lower-tier other auditors. For example, allowing the
13 first-tier other auditor, rather than the lead auditor,
14 to perform supervisory procedures for the next tier other
15 auditors.

16 Another commenter suggested requiring the lead
17 auditor to obtain information about the first-tier other
18 auditor's supervisory decisions as part of the lead
19 auditor's supervision of the first-tier other auditor.

20 Some commenters recommended clarifying how
21 proposed requirements would apply when an audit involves
22 more than two tiers of other auditors.

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 So, now we have covered the key areas of the
2 comments related to the proposed amendments on planning
3 and supervision. So, I want to move on to some of the other
4 comments and specifically we are now going to cover the
5 new proposed standard for divided responsibility audits.

6 As Dima introduced earlier in this session, in some
7 situations the lead auditor divides responsibility for the
8 audit with another accounting firm that audited and issued
9 an audit report on the financial statements of a portion
10 of a company. For example, the lead auditor may divide
11 responsibility for the audit with the other auditor if it
12 is impracticable for the lead auditor to review the other
13 auditor's work. And those divided responsibility
14 situations are relatively uncommon. As you see on the
15 slide, there were approximately 50 of these such audits
16 in fiscal year 2014. So, it is relatively uncommon.

17 When the responsibility for the audit is divided,
18 the lead auditor discloses that fact in its report on the
19 consolidated financial statements.

20 The proposal includes a new separate auditing
21 standard, as Dima mentioned earlier, AS 1206, specifically
22 for these divided responsibility audits. Proposed AS

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 1206 would maintain the requirement that the lead auditor
2 disclose in its report which portion of the financial
3 statements was audited by the other auditor or, in the
4 terminology of the proposal, the referred to auditor.

5 Commenters generally supported retaining the
6 auditor's ability to divide responsibility and provided
7 some specific comments and suggestions for the proposed
8 standard. One area, as you will see on this slide, where
9 the proposed new standard describes conditions that must
10 be met for the lead auditor to divide responsibility for
11 the audit with another accounting firm.

12 One of these conditions, under the proposal states
13 that the lead auditor may divide responsibility only if
14 the financial statements of the company's business unit
15 audited by the referred to auditor were prepared using the
16 same financial reporting framework as the framework used
17 to prepare the company's financial statements.

18 According to some commenters, such situations
19 exist today and may become more prevalent in the future
20 because of broad use of IFRS and expected increased
21 rotation of auditors involved in international audits. I
22 will also note that both the SEC Staff's Financial

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 Reporting Manual and ASB's AU-C Section 600 address these
2 situations.

3 Therefore, the commenter suggested that the
4 proposed standard allow division of responsibility when
5 the company and its subsidiary used different financial
6 reporting frameworks.

7 Lastly, some commenters recommended providing
8 certain clarifications and examples relating to applying
9 the proposed standard in integrated audits.

10 Our next slide addresses the Board's proposal,
11 including an amendment to the standard on the engagement
12 quality review, AS 1220 or currently AS 7.

13 Under the proposed amendment, the engagement
14 quality reviewer would be required to evaluate the
15 engagement partner's determination that the participation
16 of his or her firm is sufficient for the firm to carry out
17 the responsibilities of a lead auditor. And Denise
18 covered comments earlier regarding the determination of
19 sufficiency.

20 As for the proposed requirement for the EQR, some
21 commenters supported the requirement as proposed, while
22 some commenters question whether the determination of

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 sufficiency is always a significant judgment and thus
2 should always be reviewed by the engagement quality
3 reviewer.

4 Our next topic relates to a potential unintended
5 consequence Dima brought up earlier and it is discussed
6 in the Board's proposal. And this is relating to the other
7 auditor's accountability.

8 Here, the proposal would supersede, as we have
9 mentioned before, AS 1205, currently AU 543, and would not
10 retain a statement that, quote, "the other auditor remains
11 responsible for the performance of his own work and for
12 his own report."

13 To mitigate the potential unintended consequence
14 that the other auditor could feel less accountable, the
15 proposal includes a requirement that the lead auditor
16 obtain from the other auditor a written report describing
17 the other auditor's procedures, findings, conclusions,
18 and, if applicable, opinion. And Denise discussed this
19 earlier.

20 Notably, under the proposal, the other auditor
21 would continue to remain responsible for, among other
22 things, obtaining sufficient appropriate audit evidence

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 to support its written report describing the other
2 auditor's procedures, findings, conclusions and, if
3 applicable, opinion. Some commenters said that not
4 retaining a statement about the other auditor's
5 accountability in AS 1205 would imply a free pass to other
6 auditors regarding the quality and sufficiency of their
7 work. The potential reduction in accountability of the
8 other auditor, whether actual or perceived, may adversely
9 affect audit quality. For example, because the other
10 auditor could be in the best position to supervise the
11 day-to-day responsibilities of a portion of the audit
12 performed by other auditors.

13 Some commenters suggested that the Board retain in
14 the standards a statement that other auditors are
15 responsible for their work.

16 Okay, so my final area of discussion is on certain
17 aspects of economic analysis. Again, as Dima introduced
18 earlier, we will discuss certain aspects of the analysis.
19 As a reminder, the proposing release includes an economic
20 analysis that described the baseline for evaluating the
21 economic impacts of the proposal, analyze the need for the
22 proposal, and discuss potential economic impacts of the

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 proposed requirements, including the potential benefits,
2 costs, and unintended consequences. The analysis also
3 discussed alternatives considered.

4 With respect to the description at baseline and
5 need for the proposal and the proposing release,
6 commenters generally agreed that changes in the business
7 environment, company, an audit firm structure,
8 regulation, and financial reporting standards support the
9 need for change. For example, commenters agreed with the
10 need to update PCAOB standards by integrating the
11 requirements for using other auditors into the risk-based
12 approach.

13 Commenters generally agreed with the description
14 of existing audit practice in the proposal and provided
15 additional relevant information. For example, several
16 firms acknowledged that they have already updated their
17 methodologies for audits involving other auditors.

18 With respect to the description of economic impacts
19 in the proposing release, including benefits and costs,
20 some commenters provided information in support of the
21 description of potential benefits. One commenter stated
22 that the proposed amendments would provide more

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 transparency about audits involving other auditors and
2 would, therefore, benefit investors and the public.

3 Another commenter said that the proposed changes
4 should decrease the overall likelihood of misstatement by
5 enhancing the verification process of information relied
6 upon by other auditors and, therefore, should serve as
7 added safeguards for the investors and general public
8 through their ability to rely on the financial statement
9 data and related disclosures.

10 As in the example Denise gave earlier, some
11 commenters asked whether certain proposed requirements
12 are designed to be sufficiently scalable based on risk.
13 If not, the commenters caution that the amendments could
14 be unnecessarily burdensome without corresponding
15 benefits to audit quality.

16 Some commenters also caution that some smaller
17 firms could face more significant cost increases than
18 larger firms. And as a result, some firms could determine
19 that they would no longer perform audits that require the
20 involvement of another audit firm.

21 And now I am going to turn it back to Dima.

22 MR. ANDRIYENKO: Okay, thank you very much Denise

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 and Stephanie for your presentation. As you can
2 appreciate, the proposal is covering a lot of ground. It
3 touches on several key audit areas and would amend many
4 of the existing key auditing standards.

5 As I said, we asked many questions in the proposal,
6 almost 60, and we got a lot of comments. We are going
7 through these comments today. We were going through the
8 comments at the PCAOB but if you have additional comments
9 and any questions, please feel free to put up your tent
10 card and we will call on you. We had a fairly lively
11 discussion of this topic back in May, when the proposal
12 just went out, and we are happy to continue today. Sri.

13 MR. RAMAMOORTI: If you could take this slide back
14 to the reference to [AS] 1205.03, just a couple more.

15 Yes, so when I read that, it is obviously
16 gender-biased usage. So, I just want to point out that
17 I am glad that section is going out. Hopefully, you will
18 be replacing it with better language. But I should just
19 point out in general that when I first started teaching
20 in the United States, about 60 percent of my students were
21 young men and 40 percent were women. Now, it is exactly
22 the opposite. It is about 60 percent women in my classes

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 and 40 percent men.

2 And so I tell you to be very careful. Do not use
3 his or her unless you want to say he and she and all that,
4 which of course is very painful. So, I propose to them
5 a solution which I did in my Ph.D. dissertation, which is
6 make a note that this is being used as an epicene personal
7 pronoun, which means depending on context you read the his
8 as a her if that is relevant.

9 MR. ANDRIYENKO: Yes, thank you for this comment.
10 This was written in the dark days of standard-setting back
11 in the '70s. As you can see, I think you can even
12 appreciate it looking at us who are presenting at this
13 table, we are cognizant of this issue. And you will
14 probably not see it in our standards but thank you, Sri.

15 Liz Murrall.

16 MS. MURRALL: Thank you very much. And thank you
17 very much for your work in this area and increasing the
18 supervision -- your requirements for the supervision of
19 other auditors. I think that is very welcome.

20 Investors invest internationally and their
21 preference would be for harmonized requirements to apply
22 internationally for audit. But I note that whereas the

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 PCAOB is allowing divided responsibility and a reference
2 to be made to that in the audit report, the same is not
3 allowed by the IAASB in ISA 600. And, indeed, even in the
4 U.K. where we have ISA 600-plus, we go on to say the group
5 engagement partner's firm bears the full responsibility
6 for the auditor's report on the group financial
7 statements.

8 I mean both the IAASB and the PCAOB address the
9 audits of multinational companies but I question why you
10 need to have a different approach because I think for many
11 investors, divided responsibility would be seen as a
12 limitation in scope.

13 MR. BAUMANN: I will just comment on that briefly.
14 Again, it exists today in current standards in the United
15 States. So, we have put this out as a proposal to see how
16 people react to it.

17 And I think maybe Megan can comment on this. I have
18 heard, as I have sat at the IAASB CAG, as they have thought
19 about ISA 600, the group audits, that there are situations
20 where the lead auditor just doesn't have access to the
21 audit work of an equity investment or something like that,
22 which is part of the financial statements.

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 So, should the lead auditor still sign the opinion
2 of the consolidated financial statements, even though he
3 or she cannot potentially audit 100 percent of the work,
4 or should the divided responsibility exist, or should
5 there be some other solution? So, I think it is something
6 we are exploring as part of the proposal and I'm not sure
7 where we will come out on this at the end of the day. But
8 there are relatively few situations today.

9 Megan, is this something where you have heard some
10 issues at the IAASB?

11 MS. ZIETSMAN: Yes, Marty, thanks. And it
12 definitely is something that is on the IAASB's list of
13 issues. I think, as you know, we have an ongoing project
14 to look at our group audit standard and we did a very
15 significant consultation where we put out all of those
16 issues, which included some questions around the issue of
17 divided responsibility. I mean Liz is right, that [ISA]
18 600 today does not provide for the ability to divide
19 responsibility or make reference to the report of another
20 auditor in the report.

21 But what we heard -- actually, I will just take a
22 step back. When the IAASB started its project, their

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 intent was not to open up that debate because that had been
2 a very hotly debated issue when ISA 600 was first finalized
3 and I think actually was the issue that contributed to that
4 standard having to be re-proposed a couple of times before
5 it actually got finalized.

6 So, our intention was not to open up that can of
7 worms all over again but it did come out as we started to
8 explore the issues. And like you pointed out, there are
9 situations like an equity method investment where you just
10 don't have the same kind of access at management level,
11 as well as at the audit level to really be able to do it.

12 And I think actually it was at the CAG that one of
13 the CAG members put the question on the table that if you
14 have a situation where you have an equity method investment
15 that is, itself, a listed company that is audited, that
16 has a stand-alone auditor's report, that investors are
17 using to make investing decisions about with respect to
18 that company, why then would it not be permissible to have
19 a reference in the report of the company that has an
20 investment in that company to that report. And maybe that
21 would be preferable to putting the auditor in somewhat of
22 an artificial position where you really don't get the same

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 kind of access that you might when it is a component.

2 So, the IAASB has received a lot of feedback and
3 I think, like Liz pointed out, I think there is a very
4 strong view that sole responsibility is the way that it
5 should be and that we shouldn't open up this issue. But
6 the IAASB still has to go through the process of fully
7 digesting all the feedback and deciding whether there is
8 actually a narrow set of circumstances where divided
9 responsibility may make sense.

10 And the other situation that has been put on the
11 table is the situation where you have a transaction or an
12 acquisition that happens really late in the year and it
13 is very difficult for the auditor of the acquiring entity
14 to really do everything that needs to get done.

15 So, I think the jury is still definitely out but
16 it continues to be a big issue.

17 MR. BAUMANN: Your card was otherwise up. Were
18 there other things that you wanted to point out?

19 MS. ZIETSMAN: Yes, the only other thing I really
20 just wanted to point out was as I think I just mentioned,
21 we do have a project that is ongoing with respect to [ISA]
22 600. Obviously, ISA 600 is a different standard than what

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 is in the PCAOB standards. It is a standard that has a
2 lot of issues, which is what has led the IAASB to put it
3 back on its agenda. But I think the one thing that we did
4 hear in the response to our feedback, and I think actually
5 it was mentioned in the presentation the fact that firms
6 have both methodologies around [ISA] 600 and there was a
7 recognition, I think broadly across our stakeholders, that
8 [ISA] 600 has been an important standard in improving the
9 quality of the multi-location audits. So it has been
10 helpful.

11 So, notwithstanding that there are issues and
12 challenges, it is a good standard and I think we got told
13 don't throw it away.

14 But at the same time, the other project that is
15 relevant is we have a project that is focused on ISA 220,
16 which is our standard that deals with quality control at
17 the engagement level. And really what we are trying to
18 do with that one is to take the kind of principles of
19 quality management and drive that into that standard and
20 I think, actually, the work that the PCAOB has done in
21 respect to the way you have looked at this issue has been
22 very helpful to us in terms of looking at well, how do you

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 build a model that really drives the level of involvement
2 that is necessary in looking at the supervision model and
3 thinking about how it might work in different
4 circumstances.

5 So, I think a lot of the issues that we are dealing
6 with are very aligned with the issues that you have just
7 been talking about now. So, things like reliance on
8 networks. You know I think the other thing we are starting
9 to think about also is the situations where you have what,
10 at least at the IAASB, we have called audit delivery
11 models, where you have different types of engagement team
12 structures and involvement of centers of excellence that
13 may be on-shored, maybe off-shored but where you have
14 resources sitting in different locations.

15 And then the other situation, Marty, that you
16 mentioned yesterday about when the partner is not located
17 where the work is being performed and that has been pointed
18 out as a big gap in our standards as well.

19 So, I think between our two standards there -- well,
20 I think we are dealing with the same issues. So I think
21 the feedback that you have received is very informative
22 to us and, likewise, I think the feedback on our ATC is

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 very informative too to the two projects. So, I think
2 there is a lot of scope for us to think about how to solve
3 these issues together. Thank you.

4 MR. ANDRIYENKO: Thank you, Megan. Tom Selling.

5 MR. SELLING: Thanks. I am going to start by
6 stating a couple of things which may be obvious to people
7 but I think they lead to what my recommendations are.

8 It seems to me that the premise of the standard
9 is to be able to reasonably accommodate issuers that wish
10 to avoid the cost of engaging a single auditor in
11 circumstances where the costs of doing so are unreasonably
12 high or even prohibitive.

13 Accordingly, the PCAOB is proposing new and
14 untested requirements to compensate for the added risk of
15 a single auditor not performing the entire audit, which
16 recent experience has indicated is a serious risk.

17 I expect that the PCAOB's original proposals were
18 motivated by inspection results and enforcement actions.
19 So, it is difficult to predict whether the additional
20 procedures you are proposing will be cost-effective.

21 And as I said, so far, everything I have said really
22 so far is obvious but these are my suggestions. In

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 consideration of these observations, I would like to
2 suggest that the PCAOB consider an approach to rulemaking
3 that keeps its options open. For example, where the
4 comments you summarized suggest that rules are burdensome,
5 to give the commenters, initially, the benefit of the doubt
6 until post-implementation review and new experience from
7 inspections and enforcement provide information as to how
8 any new rules are working.

9 In that same spirit, perhaps the PCAOB should at
10 least consider making the proposal scalable to provide
11 extra accommodations for smaller companies.

12 On the other hand, I think that the determination
13 of who should be the lead auditor should be determined in
14 a rigid, rigorous way at all times with not a lot of room
15 for discretion by the auditor group. I think that is
16 qualitatively a different aspect of the proposal and
17 should be treated differently from a policymaking view.

18 MR. ANDRIYENKO: Thank you, Tom. We are making
19 notes of your suggestions. And of course, as I said, there
20 were many comments we received in different areas and we
21 are considering them now. I appreciate it.

22 MR. SELLING: You don't have to make notes, I have

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 it written down word for word.

2 MR. ANDRIYENKO: And we will have a transcript,
3 yes. Thank you.

4 Mike Santay.

5 MR. SANTAY: Thanks, Dima and thanks to your group
6 for all your hard work in this area.

7 Two things. One, I just wanted to mention on the
8 divided responsibility, I know we talked about that at the
9 last SAG, and after the meeting, Jeanette Franzel, who I
10 don't think is here, reminded me that the GAO is one of
11 the largest proponents of maintaining divided
12 responsibility as an option in the U.S. because it is
13 important for their audits. And as you know, they use U.S.
14 auditing standards, board-set standards for GAO audits.
15 So, it was important to them at the time to maintain that
16 because of how government audits are performed. So, I
17 just thought I would share that.

18 And secondly, again thanks for doing the project.
19 I think Megan said a lot of what I was thinking about here.
20 You know, setting standards for the private companies in
21 the U.S., we look to converge with the IASSB. We did, the
22 Board did a significant convergence project a few years'

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 back. So, our main focus is that. But we also are looking
2 to minimize differences with the PCAOB. We have an active
3 group of the Board that looks at PCAOB standards-setting,
4 monitors it, and where standards are finalized that we
5 believe would be a good enhancement for private company
6 audits, we make those changes. So, we are trying to
7 balance both. So, I think it is important.

8 And I think, Megan, you said the issues, there are
9 a lot of common issues here. And I think there some common
10 objectives, too. And really, it is about managing the
11 risks of these sometimes very complicated
12 multi-jurisdictional location audits. So you know,
13 getting the risk assessment right, getting the response
14 right, if there is other auditors involved, getting the
15 supervision right, some of those common themes are
16 resident in both projects.

17 So, I am grateful that there is going to be
18 continued informing between the two projects because I
19 think, especially from a U.S. perspective, with our
20 experience with divided responsibility and other things,
21 I think there are some good things in both projects. And
22 sometimes I think you mentioned the issues, the [ISA] 600

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 standard as it is now, it is a bit of a forest and the trees.
2 And many of the issues have been more about how do I comply
3 with the standard, as opposed to how do I do a good quality
4 audit. I know it is an inspection focus of Helen and her
5 group. So, I think that will also probably help inform
6 your project as you go along.

7 But anyway, that is my observation.

8 MR. ANDRIYENKO: We are a little overtime. I
9 think we will allow for one more comment. Phil
10 Santarelli.

11 MR. SANTARELLI: Thank you. And Mike, that was a
12 good lead-in. I have a comment and a question.

13 I was actually involved in the AU-C 600 Task Force
14 when ASB was writing that standard. And one of the things
15 that struck me, I know I have said it before, I am repeating
16 myself, but it was my perception at the time that the
17 demands that were going to be placed on what was referred
18 to as component auditors were much different than the
19 current status of AU 543. And I recommend at least
20 thinking about ways to get those other auditors that are
21 doing a significant portion of the audit and, thus, in
22 scope for PCAOB registration and rules, to consider some

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 standard-setting related to how they should relate, how
2 they should react to the principal auditor.

3 And then for Megan, I don't want to put you on the
4 spot. I know you did a post-issuance review on ISA 600
5 and you mentioned some issues have come up. Can you share
6 them with the SAG? It might be beneficial, if you can,
7 on what some of those issues were.

8 MS. ZIETSMAN: So, I probably won't get all of the
9 list of all of the issues. But I think one of the issues
10 that did come up was the challenges with respect to equity
11 method investments where you don't have the same -- where
12 the management and the auditor has the same kind of access.
13 So, that was one of the challenges.

14 I think there is challenges around component
15 materiality and how you approach that and how you set that
16 for different type of components. So, that is a
17 challenge.

18 There is challenges around the communications
19 between group auditors and component teams, and really
20 having that proper feedback loop.

21 I'm just trying to think. Challenges around risk
22 assessment and really making sure that risks at the group

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 level are driven down to the component and how you make
2 sure, as a group engagement partner, that they have been
3 appropriately responded to.

4 Challenges around different type of groups, giving
5 rise to different types of challenges, when you start
6 dividing them up into components and think about scoping
7 your work at the different levels of components.

8 So, you know I think like Mike said, I think a lot
9 of the issues are some of the same kinds of issues that
10 the PCAOB is dealing with. And you said it really well,
11 Mike, the fact that the objectives of these are the same.
12 The objectives are to really make sure that we have
13 standards that drive quality work of these types of
14 engagements, which really are very, very complicated.
15 And I think we are also in a world where they are going
16 to continue to evolve, as we look at the different types
17 of technology trends, the different types of ways that
18 entities are structuring themselves.

19 Actually, sorry, that was one other thing I
20 remember was the evolving use of shared service centers
21 by companies, as well as by auditors. And that really
22 dealt with anyone's standards and how do you deal with

NEAL R. GROSS

COURT REPORTERS AND TRANSCRIBERS
1323 RHODE ISLAND AVE., N.W.
WASHINGTON, D.C. 20005-3701

1 those kinds of situations.

2 MR. BAUMANN: Dima and team, thank you very much
3 for your comments. You did an excellent job summarizing
4 what we heard, both pro and good questions that commenters
5 raised as part of the proposal.

6 And thank you, SAG members, for the good input you
7 have given us both today and when we discussed the proposal
8 before.

9 This is a really important area. I think, as we
10 have all mentioned, we are talking about the largest audit
11 that have the lead auditor who manages that global audit
12 around the world and ensures the high quality audit, not
13 only at headquarters, but at those far remote locations
14 where there could be material operations.

15 So, we will continue to work hard on this and
16 explore next steps and look together what the IAASB is
17 doing and learn from that as well.

18