Highlights From Annual AICPA Conference

DECEMBER 30, 2013

The American Institute of Certified Public Accountants' annual conference on SEC and PCAOB developments often generates news about the thinking of key regulators. This year, much of the discussion from regulators at the conference, which was held December 9-11, was a reiteration of continuing themes. Matters of particular interest to audit committees include:

- *Accounting Firm Expansion of Non-Audit Businesses.* PCAOB Chairman James Doty and SEC Chief Accountant Paul Beswick reiterated concerns expressed at last year's conference regarding some accounting firms' expansion into non-audit businesses. Noting that "[t]he public considers audit firms to be 'gatekeepers,' and not consultants, Mr. Beswick stated, "You earn the public's trust by improving audit quality and by strengthening a firm's audit function." Mr. Doty stated, "We need roundtables and task force attention on the implications of the regeneration of non-audit consulting at the global firm."
- *Auditor Independence.* Discussing auditor independence, SEC Deputy Chief Accountant Brian Croteau emphasized that responsibility for compliance with the auditor independence rules is a "shared responsibility" between the audit committee and the auditors, not, as some may think, primarily the responsibility of the auditor. He suggested improvements to policies and procedures be considered "to help ensure that services to be provided by the company's auditor are appropriately evaluated by management and audit committees, in addition to auditors, prior to commencement." In particular, Mr. Croteau noted that the independence rules require that the auditor be independent not just of the audit client, but also the client's affiliates, and recommended that that policies and procedures make sure that the complete population of affiliates is known to the company and its auditors. He also suggested that when a company changes auditors, it consider maintaining the independence of the predecessor auditor for a period of time, in case it is necessary to audit a restatement of prior period financial statements.
- *Mandatory Rotation.* On the controversial issue of mandatory auditor rotation, PCAOB Chief Auditor Martin Baumann discussed the PCAOB's pending proposal to require disclosure of auditor tenure in the auditor's report. He alluded to the arguments about whether long auditor tenure can adversely affect audit quality. But neither he nor Mr. Doty suggested that the PCAOB expects to take any action on mandatory rotation other than the proposed disclosure requirement.

- *Audit Quality v. Fee Reduction.* SEC Chief Accountant Beswick urged audit committees, when deciding whether to hire or retain an auditor, to focus on audit quality and “not always choose the low cost provider.” He expressed concern that “audit committees may be focusing too much on the amount of the fee and not focusing enough on the expected audit quality.” Mr. Beswick suggested that in the event of an audit failure, if the audit committee was “solely fee hunting,” this might “raise questions about the diligence of the members of the audit committee in fulfilling their responsibilities.”
- *Audit Quality Indicators.* In a related topic, Greg Jonas, PCAOB Office of Research and Analysis Director, discussed the PCAOB’s ongoing audit quality indicator (AQI) project. As described by Mr. Jonas, the Board’s project seeks to answer two questions: “Can we develop a portfolio of quantitative measures that provide new insight into audit quality? If so, how can we deploy those measures in a manner that best promotes quality?” The PCAOB expects to issue a concept release on this topic in the first quarter of 2014.
- *ICFR.* Several speakers focused on internal control over financial reporting. Notably, Mr. Croteau suggested that PCAOB findings regarding inadequacies in audits of ICFR “are likely indicators of similar problems with management’s evaluations of ICFR, and thus potentially indicative of risk for unidentified material weaknesses.” Mr. Croteau also questioned whether all material weaknesses are being properly identified, noting that “[i]t is surprisingly rare to see management identify a material weakness in the absence of a material misstatement.” This view was echoed by members of the SEC Enforcement Division Staff.