Regulators Emphasize Audit Committee Responsibilities in Recent Speeches

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Chairman James Doty of the Public Company Accounting Oversight Board continued his program of outreach to audit committees in a May 2 speech on "Developments in the Relationship Between Audit Committees and Auditors" at Northwestern University Law School. Mr. Doty reiterated many of his recent themes. These including concern about the market's inability to "observe the full benefit of a good audit," which he believes results in the audit, "in the minds of some, [becoming] a rent to be contained with other tax and compliance costs;" the decline of audit fees as a proportion of audit firms' revenues; and the desirability of requiring disclosure of the names of audit engagement partners and other participants in the audit, which he believes will allow "the market to reward companies that choose audit partners with a reliable record and give others an incentive to establish one." Mr. Doty also suggested that how audit committees react to PCAOB inspection findings could affect audit quality:

> Your role as an audit committee member or counsel makes a difference to audit quality: how an audit committee addresses inspection results can affect the tone of the audit. An audit committee that is impatient with the technicalities of an audit, or accepts weak arguments to dismiss the findings in an inspection report, may inadvertently signal to the audit firm and audit team that the audit committee is not concerned with quality. An audit committee that, on the other hand, expresses explicit concern for how the auditor has resolved noted deficiencies tells the auditor that quality matters.

In a Keynote Speech the previous day, May 1, at Baruch College, Chairman Doty discussed in more detail his concerns about the impact of fee pressures on audit quality. He noted that the audit committee is in charge of retaining the company's auditor, "yet the audit committee has limited information on which to judge audit quality. Thus the primary battleground for market share becomes price." He provided statistics showing that changes in auditors results in a decrease of audit fees in the first year after the change, whereas the year-over-year change in audit fees among all companies were essentially flat. Thus, "the fight for market share becomes the fight for incumbency." Mr. Doty also seemed to suggest—at least rhetorically—that companies should explain the fee decreases:

> It is not the custom for companies' statements to explain the rationale for why a new auditor charges a lower fee than the previous auditor. Is the new auditor more efficient? Did the new auditor reduce the scope of the audit? Did the fee for the new audit cover the full cost of conducting the audit in the first year?

Speaking at the same conference at Baruch College, SEC Chief Accountant Paul Beswick also reiterated some of his prior public comments regarding audit committees. According to news reports, he emphasized the desirability of expanded voluntary disclosures by audit committees and his concern about “fee-hunting.” Most notably, however, Mr. Beswick reportedly stated that auditors and financial executives should challenge whether the audit committee is doing its job; indeed, auditors are supposed to “actually evaluate whether the audit committee is setting the tone at the top.” Past suggestions that an auditor should evaluate the performance of its boss, the audit committee, have generated concerns, and it remains to be seen if Mr. Beswick’s comments indicate a renewed focus on this issue by regulators.