NOTICE: This is an unofficial transcript of the portion of the Public Company Accounting Oversight Board’s Standing Advisory Group meeting on November 13, 2015 that relates to the Board’s Concept Release on Audit Quality Indicators. The other topics discussed during the November 13, 2015 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:
http://pcaobus.org/News/Events/Pages/Nov_2015_SAG.aspx
The Advisory Group met in the Academy Hall within the offices of FHI 360, located at 1825 Connecticut Avenue, Northwest, Washington, D.C., at 8:30 a.m., James R. Doty, Chairman, presiding.

PCAOB BOARD OF DIRECTORS

JAMES R. DOTY, Chairman
LEWIS H. FERGUSON, Board Member
JEANETTE M. FRANZEL, Board Member
JAY D. HANSON, Board Member
STEVEN B. HARRIS, Board Member
STANDING ADVISORY GROUP

MARTIN F. BAUMANN, PCAOB, Chief Auditor and Director of Professional Standards
JOAN C. AMBLE, President, JCA Consulting, LLC
THE HONORABLE RICHARD C. BREEDEN, Chairman and CEO, Breeden Capital Management, LLC
PETER C. CLAPMAN, Senior Advisor, CamberView Partners, LLC
WALTON T. CONN, JR., US Partner and Global Head of Audit Methodology and Implementation, KPMG LLP
WALLACE R. COONEY, Vice President - Finance and Chief Accounting Officer, Graham Holdings Company
JAMES D. COX, Brainerd Currie Professor of Law, School of Law, Duke University
CHARLES M. ELSON, Edgar S. Wollard, Jr. Chair of Corporate Governance, and Director, John L. Weinberg Center for Corporate Governance, University of Delaware
MICHAEL J. GALLAGHER, Managing Partner, Assurance Quality, PricewaterhouseCoopers LLP
SYDNEY K. GARMONG, Partner in Charge, Regulatory Competency Center, Crowe Horwath LLP
L. JANE HAMBLEN, Chief Legal Counsel, State of Wisconsin Investment Board
ROBERT B. HIRTH, JR., Chairman, Committee of Sponsoring Organizations of the Treadway Commission (COSO)
PHILIP R. JOHNSON, Former Nonexecutive Director, Yorkshire Building Society
JOYCE JOSEPH, Principal, Capital Accounting Advisory and Research, LLC
JEAN M. JOY, Director of Professional Practice and Director of Financial Institutions Practice, Wolf & Company, P.C.
GUY R. JUBB, 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, and Managing Partner, Sinclair Capital, LLC
DOUGLAS L. MAINE, Limited Partner and Senior Advisor, Brown Brothers Harriman & Co.
MAUREEN F. McNICHOLS, Marriner S. Eccles Professor of Public and Private Management and Professor of Accounting, Stanford University
ELIZABETH F. MOONEY, Vice President, The Capital Group Companies, Inc.
RICHARD H. MURRAY, Chief Executive Officer, Liability Dynamics Consulting, LLC
JEREMY E. PERLER, Partner and Director of Research, Schilit Forensics
SANDRA J. PETERS, Head of Financial Reporting Policy, CFA Institute
WILLIAM T. PLATT, Managing Partner, Professional Practice, and Chief Quality Officer, Attest, Deloitte & Touche LLP
GREGORY A. PRATT, Chairman, President and Chief Executive Officer, Carpenter Technology Corporation
SRIIDHAR 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
RICHARD W. ROEDEL, Public company board member
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
JEFFREY L. TATE, Chief Audit Executive, The Dow Chemical Company
BRIAN D. THELEN, Independent consultant
SIR DAVID P. TWEEDIE, Chairman, International Valuation Standards Council
JOHN W. WHITE, Partner, Corporate Department, Cravath, Swaine & Moore, LLP

OBSERVERS

GINNY BARKER, Department of Labor
BRIAN CROTEAU, Securities and Exchange Commission
BOB DACEY, Government Accountability Office
HARRISON GREENE, Federal Deposit Insurance Corporation
MIKE SANTAY, Grant Thornton
LARRY SMITH, Financial Accounting Standards Board
MEGAN ZIETSMAN, International Accounting and Assurance Standards Board

PCAOB STAFF

LILLIAN CEYNOWA, Associate Chief Auditor
GREG FLETCHER, Associate Chief Auditor
CHRIS GJETNES, Associate Chief Auditor
JANE HUTCHENS, Office of Research and Analysis
GREGORY JONAS, Director, Office of Research and Analysis
HUNTER JONES, Chief Counsel, Office of the Chief Auditor
STEPHEN KROLL, Senior Advisor, Office of Research
GREG SCATES, Deputy Chief Auditor
EUGENE THERON, Associate Director
JOY THURGOOD, Associate Chief Auditor
BARBARA VANICH, Associate Chief Auditor
JESSICA WATTS, Associate Chief Auditor
GEORGE WILFERT, Deputy Director and Senior Technical Advisor, Office of Research and Analysis
KEITH WILSON, Deputy Chief Auditor
MR. BAUMANN: Well, good morning, everybody and welcome back to day two of the meeting of the Standing Advisory Group.

Tremendous energy yesterday in the breakout sessions both with respect to audit quality indicators and the emerging issues and certainly with respect to AQIs. You gave us a lot of information to consider regarding our next steps and we'll be talking about that in a moment. But also regarding the emerging issues.

You gave us a lot to think about in terms of potential actions or alerts or guidance that we may have to give out with respect to audits and some of these emerging issues and we'll be talking about that after the break.

So we appreciate the energy and all the ideas yesterday and let's keep up the high level today. So with that, I'll turn it over to Greg Jonas.

MR. JONAS: Thank you, Marty. Good morning, everyone.
First of all, thanks for the great discussions in the breakouts yesterday. All the moderators reported highly interactive and engaged discussion.

I think we have some important things to tell you about those discussions and let me tell you how we'd like to spend the next 90 minutes.

First, we'll debrief the three breakout sessions going breakout group one, two and three in that order. The moderators will speak for about five minutes using some slides to summarize what we believe to be the main takeaway points from those discussions.

Following each moderator's summary, there will be about five minutes or so for members of the breakout group to add color as you deem appropriate to what the moderator might have said.

Then after about 30 minutes after the debrief of the three breakouts that will leave us an hour to go around the room and hear from each of the SAG members on your personal advice to the board on what counsel you have for next steps that you believe the board should take on the AQI project.

We hope that your advice would concentrate on the
kind of short term, what should the board do in the next year, if anything, and that your advice be directed directly to the board, so not so much what should audit committees do, what should audit firms do but rather what should the PCAOB do, if anything, with regard to the project.

Okay. So with that, let me turn it to breakout session one for a summary of what was discussed.

MR. THERON: Thank you, Greg.

Our plan in group one was to discuss the proposed listing of AQIs within the concept release and its content without regard to who the customer of that information is.

However, our group quickly determined that the question of whether a standard set of AQIs can be assembled or what the optimal number of AQIs might be or even which AQIs are most promising and effective depended in large part on who that customer is - audit committees, regulators, investors, it is not necessarily a one size fits all.

Take action. Most in our group felt that further debate was no longer constructive and that the PCAOB needed to get going on this and take action, the overarching
premise being that AQIs would in fact be useful.

   In fact, some audit committees and their auditors are already doing this. The view around our table was that the PCAOB is in a unique position to provide valuable insights and certainly some context and that the PCAOB should inform while audit committees decide.

   While there clearly is a desire for additional information, data, empirical analysis about AQIs, our group believed that the data would begin to tell the story over time as this gets rolled out and that the AQIs therefore would evolve over time.

   George?

   MR. WILFERT: Thanks, Eugene.

   First, the group was generally in favor of the PCAOB developing a framework using a principles-based approach, organized in a manner similar to the broad categories outlined in the concept release, such as under the category of audit professionals, for example, having sub-categories for availability, competence and focus.

   However, as Eugene noted, the group also noted that various AQIs may have different levels of relevance for different users, who may also have varying levels of
context available to them.

Therefore, the general view of the group was that allowing flexibility for users such as audit committees to be able to have the discretion to choose from a menu of AQIs would be preferable.

In addition, audit committees and other users may also want to add other AQIs they believe are relevant and tailored to the circumstances of their audit.

The group generally was in favor of the PCAOB providing common definitions of how to calculate various AQIs in order to promote comparability.

There was also the caveat that audit quality indicators are only one of many tools available to audit committees and that they are not benchmarks, scorecards or a panacea to improving audit quality, rather, that their greatest use may be as generators of questions for auditors leading to a more robust dialogue about audit quality.

The consensus of the group was that it was too early to determine whether there was an optimal number of AQIs that could be used to inform discussions about audit quality. However, the general view was that 28 indicators was too many.
Eugene?

MR. THERON: Thank you, George.

Next slide please, Brian. From the investors in the room we heard a clear request that AQI information - a clear request for AQI information following a phased rollout.

Others in the room were concerned whether investors will in fact have the appropriate context. Though we didn't reach a consensus on this, we did discuss a range of possibilities to meet investors' requests for information, ranging from the audit committees certifying that AQIs have been evaluated in connection with their auditors' appointment and performance all the way to full disclosure of the subject AQIs.

So that's a very high level summary, in a nutshell, of what we thought was a very good discussion in group one and I'd like to now open the floor and invite members of our group one discussion to weigh in with any added color or comments, if you have any.

MR. BAUMANN: Sri Ramamoorti.

MEMBER RAMAMOORTI: Good morning. One of the comments I had made as I was a member of group one was that
we might usefully draw a parallel to the concepts of planning materiality and evaluative materiality and think about planning stage AQIs that will give an idea about audit quality and evaluative stage AQIs that will give us an idea about a quality audit.

So the planning stage, you know, is more of an input consideration and the evaluative stage is more of an output-outcomes consideration.

So that might be a useful way of thinking about AQIs.

MR. BAUMANN: Thank you, Sri. Walt Conn.

MEMBER CONN: Thanks, Marty.

One thing I would like to add, I think our discussion - I think there was a consensus that not only are AQIs dependent on the broad user group, i.e. audit committees, regulators, investors, but they are also unique to a specific entity and their audit committee and therefore I think the consensus of the group was that the PCAOB at this time should not mandate use of any AQIs that are in such a framework but rather let auditors and the audit committees decide which ones are relevant to that entity.
And I think that got some validation from Joan Amble's experience in piloting some of the 28 that were in the concept release and they added some and used some that were in the concept release.

MR. BAUMANN: Joyce?

MEMBER JOSEPH: Thank you.

I just want to elaborate a little bit more around the points that we had discussed in the group yesterday. And that is, it's clear that U.S. accounting standards are directionally taking a principles-based approach in its rule making for good reasons and a path to consider taking forth the use of AQIs could potentially be a principles-based approach as well.

That is, under a proposed framework of the three categories, audit professionals, audit processes and audit results, and the PCAOB providing a slate of AQIs with definitions and allowing the use of the AQIs amongst audit committees to be flexible, as over time the audit committee members determine which AQIs are most relevant to their company, given the particular needs, the facts and circumstances, and allow it to evolve based on the organization and the audit and also allow time for that
process to gather actual data regarding AQIs and how they provide the best indicators of quality.

Based on that information, based on that data, over some appropriate period of time, a phase-in period, consider identifying a core set of AQIs that potentially could be made public for investor decision making with investor input in that determination.

MR. BAUMANN: Liz Mooney.

MEMBER MOONEY: Thanks, Marty. Just on the mandate point, I think that we just need - we need more data before we can really decide on that. I think if we had more data - were more informed and could back test, look at some of these AQIs, I think we could probably come to a conclusion that some of them are quite useful and I would expect it would improve our data quality if there was a standardized measure and mandatory AQIs.

MR. JONAS: Okay. Let's, for the second time, move to breakout group two. The subject of discussion was auditors' discussion of AQIs with audit committee.

Brian, the next slide, please. So on points of general agreement, the first point was nearly unanimous. Auditor discussion of AQIs with audit committees “would”
be useful.

This is a stronger statement than we have traditionally made. We have always used the word “could” be useful. But the group was comfortable using the stronger word would.

If we said could it would be a unanimous view, that they could be useful. But a strong majority all but two felt that it would be useful.

The rest of the points of general agreement are a strong majority but not unanimous. So one, two or three members really had different views. So we don't mean to present this as unanimous.

But strong majorities felt that engagement level AQIs are most useful for audit committees. The audit committee is first and foremost concerned about their audit team's performance than they are about the firm over all.

That said, the group felt that firm wide level AQIs did have a place but their place was to provide context for the discussion of the engagement level AQIs.

The next point is any discussion of AQIs should be determined by audit committees and firms. Let me
emphasize the word “any”. That means the group was in favor of a purely voluntary regime.

That is, audit committees and auditors would decide whether there's any discussion of AQIs at all and if there would be a discussion what the content of that discussion would be.

The group felt that firms should be free to disclose, as they are today, firm level AQIs as they deem appropriate but felt that firm disclosures of firm level AQIs would be useful to provide context for AQI discussions with audit committees.

So some of you may be wondering then in a purely voluntary regime - if we could move to the next slide, thank you - what is the role of an audit regulator in a voluntary regime and our answer is as follows.

First, to share insight on possible useful AQIs. So the regulator could say what we think might be useful and that that insight would come largely from our inspections experience.

But they had two caveats. First, we would need to be very careful in offering what we believe to be useful AQIs to avoid doing so with any implication that they would
be required to be discussed and we should do everything we could to not add to an already high legal risk facing audit committees.

The next role for a regulator is based on two ifs. If an audit firm provided - decided to report to the public on its audit quality - and if that firm elected to include AQIs in that reporting, then it would be appropriate for a regulator to say; then you will define the AQIs as follows. So be prescriptive as to if you make the decision to disclose them you would have to follow a certain way of calculating them and the benefit of that would be some consistency and some common understanding of vocabulary and terms across firms.

But at a minimum that if firms voluntarily disclose AQIs they should disclose the way those AQIs are calculated in the event that the regulator did not prescribe how they would be calculated.

So the group was very much in favor of full transparency by firms and voluntary reporting of AQIs.

Two new ideas came up in our discussion. These were not points of consensus. In fact, there was some disagreement about them. But I mention them because they
were different than what we had put in the concept release.

The first is the notion of mandating discussion of AQIs but without any prescription as to what the content of the discussion would be. And the second idea was based on the fact that AQIs have become a global sport. Many audit regulators around the world are considering AQIs as are the major global firms on a global basis.

And the thought was to avoid having each audit regulator in various regimes kind of doing their own thing on AQIs, sending potentially conflicting and confusing signals to the market. So this is a notion of a desire to have some coordinated type of AQI policy across regimes.

So with that, let me open it to breakout two group members to add any color you'd like to these - this summary.

MR. BAUMANN: Chairman Doty.

CHAIRMAN DOTY: I think it leads to an interesting question. Was it - was it a consensus or a view in breakout group two that if the PCAOB exceeded or went beyond the limited role that you described that we would actually be working counter to our objective clearly stated to empower and to enhance role of audit committees.

MR. JONAS: I would invite members of group two to
weigh in on that question.

MR. BAUMANN: Bill Platt.

MR. PLATT: Well, Mike was going to weigh in on the question so I'll give the floor to him first and then I'll - and then I'll speak.

MEMBER GALLAGHER: I'm not sure I have the answer to the - I'm not sure we considered that. I think the reticence around having a requirement at this point of specific AQIs in particular and having a more hard wired approach by the regulator at least was premature, given where we are in the journey, and that there may be a point as this process matures where the role of the regulator could be enhanced and go further.

But I think that there was such broad support that this got off to such a good start and is stirring such a good dialogue we don't want to ruin it by having - by being too heavy handed-at least at this stage of the journey, Jim. That was my take. Others can comment as well.

MEMBER PRATT: Yeah, Mike. I think you said that well. I think as we - we did talk about in the - in the group to the extent that you have a prescribed list that's not viewed as being all - totally-relevant to an audit
committee that you run the risk that it becomes more of a compliance exercise rather than achieving the purpose we are looking for which is really to provide information that's a catalyst to a discussion about managing in essence the performance of the audit to deliver high audit quality and therefore focusing on things that the audit committee felt were valuable would enrich that discussion and not cloud it with things that they felt were just compliance activities.

So I do think that yeah, we did feel that it could be detrimental if you came up with a prescribed list at this point.

MR. BAUMANN: Just following up on Jim Doty's question and the point - bullet number one up there about, let's just say, AS 16 were amended to require the auditor discuss with the audit committee indicators of audit quality that should be - could be considered or discuss with the audit committee what the audit committee viewed to be appropriate audit quality indicators.

Did that get - that wouldn't describe a list but let's just say top quality audit committees today are discussing audit quality indicators but maybe not all of
them are. Would such an amendment cause any problems or
any inhibition?

MR. JONAS: Yeah. Marty, I think we specifically
engaged in that discussion in terms of could AS 16 be
amended and include this.

I think that was viewed negatively, certainly by
members of the audit committee that were in the group that
this is one more required communication rather than giving
us the latitude to, you know, decide how we're going to
spend that limited amount of time.

The other thing we talked about, again, is that if
you're going to have audit quality indicators, whether
they're mandated or not, and our preference was certainly
not mandated, is the importance of integrating the
indicators in the discussion because I think you'd find
that most of the indicators that would be useful would
probably be tied towards something that's already a
required communication. It would just enrich the
discussion around those items. So bolting it on and
saying in addition to the required communication is you
also have to do, you know, a certain number of audit quality
indicators I think was viewed very negatively.
MR. BAUMANN: Chuck Senatore.

MEMBER SENATORE: Just to follow up on something that Mike said. I think that there's no real disagreement about the value of the discussion.

One thing that struck me in the room is that it seemed as if the audit committees and the firms represented in the room didn't need the help maybe that some audit committees that might not be of the same provenance might need.

So there's clearly a need to have - promote the discussion. But the other point at least that struck me was that many times a highly quantitative approach, you know, with certain sort of rifle shot indicators, there's a danger of kind of getting information but missing the view in terms of the point of context.

I know that the proposing release talked about the importance of context. We talked about the importance of context in the meeting and perhaps, to Mike's point, as experience unfolds, as we begin to perhaps learn through the exam and the examination experience that the PCAOB does and sort of maybe see higher correlations between certain audit quality indicators and actual great outcomes.
Then maybe we'd be further down the road towards actually mandating something or suggesting strongly something that could actually - that we know will actually provide value.

You know, I think there's maybe a little time that needs to unfold before we get there.

MR. BAUMANN: Sara Lewis.

MEMBER LEWIS: Hi. So from the perspective of an audit committee chair I would say that, you know, several of the indicators in the list we actually already receive information on and so - and we use those in the process of our annual auditor evaluation.

And so that, I think, is the appropriate time to look at these audit quality indicators. But the reality is is that I believe you get much better information from your qualitative discussions with your auditors throughout the year, you know, throughout the quarter, throughout the year and also from the management team.

And I can tell you, you know, quantitative numbers are not ever going to replace the importance of the qualitative discussions and quantitative measures in my mind are generally backward looking and really are not
going to impact my particular audit, I don't believe.

And so I think that they're a useful tool for a
discussion but I think that what might be more useful is,
you know, the firms that provide transparency reports if
they're able to evolve their metrics over time to give us
a view of how the firm is addressing quality issues
themselves I think that that might be more useful going
forward than a prescribed indicator that might not be
useful in the future.

MR. BAUMANN: Phil Santarelli.

MEMBER SANTARELLI: Thanks, Marty. I would just
differ slightly from Mike's comment. I don't think AS 16
would benefit from a requirement to have an audit quality
discussion with the audit committee.

However, it might benefit by having a suggestion
in the - in the planning phase of discussions with the audit
committee that the auditor should make - should offer to
- or suggest to the audit committee, if they want it, the
ability to have an audit quality indicator discussion and
report out at the end of the engagement versus a mandate.

But kind of to Chuck's point about another way to
influence audit committees that may not be aware that this
is something they should be considering to kind of move it down that needle.

But I think a mandate to have a required disclosure and negotiate it I think would be more of an option that could, I think, be baked into AS 16.

MR. BAUMANN: Thanks. And I guess we have world class audit committee members on the SAG and not all audit committees are of the same talent that we have at this group right here. So that's why there may be some different - potentially different views there.

MEMBER GALLAGHER: Marty, I would just say that opening up AS 16 to tell auditors that they have an option to communicate. AQIs doesn't seem like the highest and best use of our standards.


MEMBER ROEDEL: Thank you. There was a contrarian view in breakout group number two about mandating AQIs.

I believe they should be. I believe they should be mandated by the PCAOB who has a seat at the table high enough to see the landscape and can, I think, play a part in deciding what those AQIs - the best use of those AQIs
and what they are, remembering that they're a tool amongst many tools that audit committees have to assess the quality of the performance of its outside independent auditors.

But that's not my point. The larger issue that I think needs to be addressed is how the firms and not just the big firms but all firms that service public companies need to speak to both the users of those financial statements and the consumers of those audit services about what they're doing to improve audit quality.

Now, the big firms, many represented here in the room - Pricewaterhouse, Deloitte, Ernst & Young - all do that through the transparency reports that they issue.

Some have suggested that they could be improved. Maybe there's a little bit more salesmanship in those documents than needed to be but you could be prescriptive in their contents.

But my suggestion - my strong suggestion would be to at some point in time think about requiring those firms to go on record each year about what they're doing inside their organizations to prove - to improve quality.

That would be very helpful and as a subset of all of that particular AQIs that would be particularly helpful
to audit committees. While it is critically important that the audit committees understand the people who are actually rolling up their shirt sleeves and doing that audit, their experience, their independence, their knowledge of the company and its industry, while that's critically important it is also important - I'd add critically important - that the audit committees understand the environment in which those teams operate. So it's very important for them to understand what the firm is doing to improve quality throughout the entirety of its organization.

So I - while it is not necessarily a subject for today, I think in the longer term, users of financial statements, investors and audit committees would benefit by the firm speaking to them about what's going on in their practices with respect to the improvement of audit quality to which we're all significantly interested in.

MR. BAUMANN: There's two cards up. Can we take these two and then move on to the next one? Bob Hirth and Philip Johnson.

MEMBER HIRTH: So, Marty, if it was decided you didn't change AS 16 so there wasn't a mandate, I think that
you do have a bully pulpit with respect to a lot of the publications you come out with and a great example to me is the audit committee dialogue.

And it got plenty of attention so my idea here would be wouldn't you maybe develop an audit committee dialogue piece.

I kind of like those words, and now it's on AQIs and you have got a tremendous amount of material already around all the background, all the work that Greg has done. You could talk about the SAG input and the things we learned here, give all the background and rationale, show the example measures as example measures and then by doing that you end up, I think, picking up a lot of media attention.

You know, Compliance Week will write about it. I think you could make sure you get it to the NACD, AICPA. They will all write about it. The large accounting firms will probably also write about it because it's issued to inform their clients what they think.

So maybe it's the audit committee dialogue that's the way to get it all out there in a broad enough way that, you know, more and more audit committees and companies might pick up the idea and do something.
MR. BAUMANN: Philip.

MEMBER JOHNSON: Thanks, Marty. We had an excellent discussion and the summary does reflect what was said and the other comments.

I think most of the - if not all the - audit committee members and chairs felt that it was at engagement level that it was particularly important, the interaction between the client and the auditor is very important, and I think also that the concern that certainly I have and I there were others had a similar concern that if we just focus on quantitative measures, hard measures, then the less informed audit committee will see that as the measure of audit quality and it isn't because there are, and it's been articulated around this table, there are lots of qualitative measures - the outputs, the interactions that - as a consequence of those softer indicators, you get a good feel as to whether it's being a quality audit or not.

And unfortunately, from my perspective, the concept release solely focused on quantitative and it was only mentioned round about two-thirds of the way through that there were other aspects that could influence audit quality. So I just think that the board just needs to
consider the focus of these indicators.

But I think undoubtedly there is a need for audit quality indicators to be out there. There are nine initiatives, however, and some range around the world and there are - and they range from six audit indicators to 40.

That's not a good place to be when we're talking about, particularly when it's the larger - as Greg said yesterday, it's the larger firms and the larger companies that are really impacted here.

And so we need to make sure that we do have some joined up writing on a global basis.

MS. HUTCHENS: So we're going to take a sharp right turn here because breakout session three had very different views from breakout session two.

There was general agreement in four areas. While not unanimous, it was a majority view as it relates to the use of AQIs by investors. These were the four general areas of agreement.

First, there was an agreement that the end goal should include some level of mandated disclosure to investors.
Secondly, the majority of investors or the view was that the majority of SAG members agreed that investors are capable of evaluating AQI metrics in context. In some of the comment letters that were received there was discussion around whether investors could absorb the AQI metrics in the context and have the appropriate context to understand those AQI metrics. Those in breakout session three felt very differently and said investors on a regular basis are reviewing very complex financial statements and therefore would have the skill set necessary to understand AQI metrics and the related context.

Thirdly, there was consensus among the group that narrowing of the 28 AQIs is necessary to cull out the most valuable ones. So as Philip mentioned, narrowing that list down to those that are most valuable.

And lastly, in the area of general agreement our group recommended a phased approach with a bias for action and that would begin with a core set of AQIs specifically around audit team mix, the competence and availability of the audit team, and then there was also discussion in that phased approach that the PCAOB should continue evaluating AQIs through research, monitoring of the practice of AQIs
currently available and through outreach.

In our next slide, we've presented three areas in which our group had controversy or just did not have general consensus.

The first related to the length of time for which phasing should last. There was varied discussion in this area.

Some would say one to two years, some would say three to five years. So we were not able to reach consensus in that area.

Secondly, the nature and extent of the testing to be performed. We lacked consensus in that area. And then lastly, there were various opinions and suggestions on the ways in which AQIs could be disseminated. Lots of ideas came out of the room.

Unfortunately, we weren't able to give you a consensus on what everyone agreed but we had lots of good ideas around the ways the AQIs could be disseminated.

Lastly, we had four new ideas out of our breakout group in this last slide, the first relating to the relationship between AQIs and CAMs, or critical audit matters.
An example was brought up in our breakout session. If you have a critical audit matter specific to an industry, it could be relevant to also understand an AQI measure related to the industry expertise of the audit team itself and their ability to handle that critical audit matter relevant for that industry.

Second, the idea was to have separate work streams for the firm level AQIs from the engagement level AQIs. There was some discussion that there's been further progress in firm level AQIs, especially given that many firms are already publicly disclosing firm level AQIs and maybe that we are still progressing along on the engagement level AQIs but we should not let the progress of our - or we should not let the progress of the firm level AQIs impact our progress in the engagement level AQIs and vice versa.

Our third area here was to disclose firm level and engagement level AQIs in separate documents. There was some discussion around this new idea that commingling the disclosure of these two in the same document would not be preferred but to rather disclose them in separate documents.
And the fourth idea was around the value that can come from looking at trends of AQI data over time and that can be just as valuable as evaluating an AQI for an engagement level-specific audit and comparing that to another audit or firm versus firm.

So we talked about time sequencing and the trends in those AQIs - in that AQI data being just as valuable. So I'd like to open it up to anyone from breakout session three that would like to add color to those points or key takeaways.

MR. BAUMANN: Brandon Rees.

MEMBER REES: Thank you.

I agree with your assessment that if breakout session two was from Mars, session three was from Venus and we were very, very eager to see AQIs disclosed to investors, investors being the ultimate third party intended beneficiaries of audits that they should receive audit quality indicator data through mandated disclosure of engagement level AQIs.

And we identified, I think, three potential areas that AQI information will benefit investors. First, proxy voting - issuers in the United States trust their
share owners to vote and ratify their selection of the independent auditor at annual meetings and yet investors are given zero information about the quality of the audit and that this would be a very beneficial corporate governance mechanism to enhance audit quality indicators by improving proxy voting.

Secondly, improving and assisting with shareowner engagement with boards of directors and audit committee members in discussing audit quality to have some concrete information that investors could dialogue about.

And then thirdly, securities analysis - that investors - not all investors will trade on AQI type information but it will help investors better appreciate the risk of a material restatement and that by having that information priced into securities will reward companies with high quality audits with higher stock prices.

The - to add some color about where AQI information should be located and disclosed to investors, there was differing views - should it be in the audit committee's report to investors in the proxy statement versus in the auditor's report.

One view was that the auditor's report - that AQI
data is the auditor's information and it most makes sense to be disclosed through the auditor's report.

I don't think it's - my personal view is it's not necessarily a - in conflict you could have auditors disclose this information to investors and then have the audit committee discuss their assessment of that information in the proxy statement. So I hope that's helpful.

MR. BAUMANN: And I guess if it was discussed - disclosed through the auditor's report then the PCAOB would have the authority then to get that information to investors because it's coming from the audit report and not the proxy statement necessarily, I think, was part of the issue.

MEMBER REES: That's right, and I would - my personal view is that as the specialized agency that has the benefit of inspection reports and the data that the PCAOB does gather from its oversight of the audit process that the PCAOB is best in position to identify those AQIs that should be disclosed to investors that are most material.

MR. BAUMANN: Tom Selling.
MEMBER SELLING: I want to emphasize the point that narrowing the range of AQIs that the board would consider from 28 to, say, four or five would really catalyze the project and I think that was one of the most valuable suggestions to come out of our meeting.

Among other things, it would enable us to start the process of documenting and validating the benefits of AQIs and my personal vision is that AQI reporting could eventually look something like the way that MD&A has evolved in that there might be tabular - required tabular disclosures of certain quantitative information but also there would be a mix of required and voluntary qualitative information surrounding that to provide the context that a lot of people feel is sorely needed.

MR. BAUMANN: Joan Amble.

MEMBER AMBLE: Yes. I wasn't on that panel so is it okay if I offer a question?

MR. BAUMANN: Yes, it is.

MEMBER AMBLE: Okay. I'm intrigued and don't agree with the view just expressed. But is the presumption if it's mandated, and I'm not sure which of
the ones that are being - that were being suggested in this
group be mandated and provided to investors - would the
presumption then be that they would have some sort of
controls around them and they would have to be audited,
number one?

And is it - is it the quantitative data only that
you're asking for or would it be the - I mean, what I have
found through trying this out is the most important
element, which has been discussed, is the qualitative
elements to it and the trend analysis.

But are you thinking - is the group thinking of a
point measure required and would it have to be audited and
have controls around it and would that have to be
regulated?

MS. HUTCHENS: I think in our group the four that
were brought up were some of the first measures. One,
five, six and seven were the actual ones that were brought
up.

But specifically related to the audit team, the
competence and the availability, we did not specifically
discuss your question. So if there's someone from our
breakout group that would like to respond to that question.
MR. BAUMANN: The question was would the audit quality indicators included in the auditor's report have to be audited. I think that was touched upon. I think some folks didn't think so. But I don't know. Does anybody - Brandon, do you want to comment?

MEMBER REES: Well, there was a discussion about the value of having standard definitions to enhance comparability and I think also identifying a certain core set of AQIs that, again, would enhance comparability, comparing between issuers in the same industry, for example, would be very beneficial.

And I don't think any investor would take the view that they would only want the quantitative data. They would also very much appreciate a qualitative discussion, a narrative discussion, of the quality of the audit and interpretation of that AQI data.

MR. BAUMANN: Sir David Tweedie.

MEMBER TWEEDIE: Thanks, Marty.

I think one of the advantages of getting older is you don't actually care what you see and having been a standard setter, I notice the constituents fall into one of two categories.
You either get the conservatives who say don't do it or you have the liberals who say do it but not yet.

And there's all sorts of things that you can do. You can do more research. You can do field tests. You can do more consulting. You can re-expose, anything that delays the project.

Looking at this, I see it fairly clearly. I'm not terribly interested, to be honest, in firms' transparency documents. A lot of them have got a lot of puff in them, talk about centers of excellence. Well, nobody has centers of mediocrity, not that they boast about.

Audit committees, yes, their information is good for them. But I don't like the idea of the audit committee telling me on the outside what they think I might want to know.

What I would like to know is when I look at this audit and look at the financial statements I want to know can I trust them - is there someone like Mike Gallagher running this audit.

Now, I know I'm going to have to go rummaging through several pages to find out since it's not going to be in the audit report but basically looking at that I want
to know what the audit team is like.

I want to know the makeup. Is it senior people? Are they specialized if we're dealing with banks and valuation issues? Are they specialized in that? Have they called specialists in? What's their industry experience? How long have they been on this sort of engagement? That tells me a lot about the team. It also helps when I look at the critical audit matters.

As I said, the fact that you can then see that one of the audit's critical matters was valuation. What have they got on the team to deal with that? Is it a bunch having a go at it or is it someone who really knows what they're talking about.

It also helps, I think, with the - if in the event the audit changes and there's been some sort of lower fee how are they going to meet that? Are they going to match the team that's just left and that's a sign which I think the audit committee would then feel very strongly about and hopefully the fact that they're going to have to publicize it would actually maybe stop some of that happening.

Industry levels, I think you could build up. The
PCAOB could collect and collate the data from this and then decide that for banking this is a normal or the median breakup of the team and so on so you can compare that to another.

But what it's doing is what I think this organization is meant to do is to be giving me confidence and the numbers I'm going to look at are right and I don't think I need the audit committee to tell me what is there.

Those four audit quality indicators would give me a lot about the team and that's really - we can develop it later. Some of these 28 have gone into the stratosphere and fine, they can be developed later.

The audit committee will find things like training, et cetera, useful. But as far as the actual accounts are concerned I think knowing the experience, the type of people who are on that and the prime auditors are going to give me a lot more information and confidence.

So that's why I'm all for putting it and I would go on with it now unless you want to be another liberal and yes, but not yet.

MR. BAUMANN: Thank you, David. Sri Ramamoorti, and we have - I know Greg wants to have a discussion around
the room so we have Sri, David Kane and Jeremy Perler.

MEMBER LUKOMNIK: Could we have the people who
were on the breakout group speak first?

MR. BAUMANN: Pardon?

MEMBER LUKOMNIK: Could we have the people who
were on the breakout group?

MR. BAUMANN: Sure. John? Jeremy Perler was in
the breakout group? Okay. John.

MEMBER LUKOMNIK: I think that the reason that
this group came up with such different results and I'm
sorry Joan's not here to hear it is that Sir David earlier
on suggested narrowing the discussion around those four
indicators.

They are, I believe, much less controversial, not
universally applauded but materially less controversial
than looking at all 28.

It was my suggestion that we bifurcate. Sir
David's was even more limited and I think that's a very
good thing and to his plea to just get on with it I would
suggest that by narrowing it to the least controversial
that becomes part of the testing phase but in a mandatory
disclosure fashion and it is hard to argue that the amount
of staff, the expertise of staff, the specialization level, particularly when you can cross it with a CAM.

And I apologize for my voice. It is not useful and it is something that would be beyond the ability of investors to understand or to put into context.

And so I think that in some ways the - when you look at the entire concept release there are things people can argue about and to use Sir David's view, don't do it or don't do it yet.

When you narrow it to these four specific this breakout group could come to a consensus to say yes, this could move forward and this could be useful and it can in effect serve as the basis for part of the engagement level gathering of information even while providing information.

So I do think it is important that when you look at why we took a different view, it is because we were looking at a set of indicators that I think there was fairly universal agreement upon.

MEMBER PLATT: Jon, just one question. I'm sorry to go out of turn. What are the four, just for the rest of us, because it might be insightful.
MEMBER LUKOMNIK: One, the staffing leverage, five, the persons with specialized skills and knowledge, six, the experience of audit personnel and seven, the industry expertise of the audit personnel. So those are fairly down to earth important pieces of information.

MR. BAUMANN: A couple of others who were in the room had their card up. David. David, you were part of this.

MEMBER KANE: Yeah, Marty. Thanks. Yeah, I think there was some general agreement that AQIs could benefit investors over time but I do think taking a parallel path with both engagement level as well as firm level does make some sense.

On the firm level transparency reports, I personally do think it's important for the investing public to understand what the firms are doing in terms of their quality agenda, focus areas, their infrastructure to support delivering quality audits and I think some of the firms have already got some of those publications out so the PCAOB could continue to foster and encourage that type of information to be disclosed, have it on firms' websites, make sure it's accessible to investors.
I think, though, on the engagement-specific piece, one area of caution is just that while there may even be some agreement about some of the specific metrics, again, just putting those out there without having the context around them could actually be more harmful than beneficial, you know, when taken out of context there.

So, we have to really kind of think through that a bit more and one way to do that would be, as has been discussed before, talking to the audit committees, maybe even about these specific ones, what sort of discussions were engaged with them -- what was the appropriate context.

I think the PCAOB could do something like that FRC did in terms of the best practices document out there on auditors' reporting. That was helpful not just for auditors, but also for audit committee members.

We think about these AQI discussions they're going to be very rich, I think, between auditors and audit committees.

So giving audit committees and even auditors the benefit of what some of those discussions look like, what some of the metrics are I think will help narrow that down a bit more and, at the same time, help raise some of the
MR. BAUMANN: Thanks, David.

We want to take -- Greg wants to get on with a further discussion but Maureen McNichols was also in this particular breakout room, and your card is up.

MEMBER MCNICHOLS: Thank you. I was just going to comment that sort of the discussion around a voluntary approach doesn't get you to getting information to investors.

There's sort of no clear path to getting information to investors along the lines that is needed, is demanded to, sort of, better understand the quality of audits and understand the quality of the financially reported numbers.

So I think that was a major argument for moving ahead and the idea of starting with a few -- a few metrics like one, five, six, and seven.

I think the notion of phasing in was you start there and see how that information is received and then work further to develop additional indicators that investors and audit committees can use in making decisions about audit quality, engagements, and, sort of, investing.
decisions ultimately.

Joan Amble asked the question about whether these numbers would be audited, these AQIs. To the extent they come from the audit firms, these aren't assertions of management and wouldn't require auditor controls. So I think that was all I'm going to add at this point.

MR. BAUMANN: Thanks, Maureen.

And the last card Sri, if you could make it short.

MEMBER RAMAMOORTI: I want to clarify that I was just trying to jump the queue, because Joan was given the license earlier.

I will be quick. There's a 1999 white paper from the Scottish Institute that talks usefully about disclosure philosophy by distinguishing between expert and inexpert investors when it comes to reading and interpreting financial statements.

The same kind of comment could be made about expertise on audit committees. Not all audit committees are created equal. So I think if we do go ahead with mandating anything, I think it is probably advisable to provide guidance, so that the folks who aren't exactly expert are able to interpret the information. That's all
I want to say.

MR. JONAS: Well, thank you for that and thank you for the debriefs -- each of the groups.

What we'd like to do, lastly here, is go around the room and get your personal advice to the board. Just to frame it, though, having issued the concept release, having had the benefit of the comment letters, having had the benefit of this discussion, I think the board finds itself at a bit of a crossroads here with the project, needing to take decisions about next steps, if any. And so I think your advice is particularly timely to the board.

So Marty, wherever you'd like to start. Our dilemma here is, you know, with the number of SAG members we have, the budget for your comments is literally one minute, and I am sorry for that, but if you can try to be concise with your comments, I know all of your fellow SAG members would appreciate the opportunity to speak as well.

Marty, where would you like to start?

MR. BAUMANN: Well, Philip Johnson, I just was looking right at you, so we'll start with you and go to your left.

MEMBER JOHNSON: Okay. Thank you.
Not much thinking time. I think -- I've said most of what I said -- wanted to say with my earlier comments. But I think I -- first -- I think about being cautious about having too many indicators, that too many hard measures. One of the issues about hard measures is people manage their businesses to those hard measures and that's not really where we want them to be with regard to quality indicators.

Certainly, I don't believe they should be mandated, and I had also mentioned about qualitative as well as quantitative. There is a combination there.

But I think 28 is far too many and people will report -- it will become boilerplate reporting. It really won't tell us an awful lot about quality and it does -- it is important that we do look at those audit committees that don't have the expertise that is being expressed around this -- from individuals around this table.

MR. BAUMANN: Harrison Greene.

MR. GREENE: I don't really have anything to add, but I did like Bob Hirth's idea about putting out a paper, which could be done a lot easier than, I guess, standard setting.
MR. BAUMANN: Wally.

MEMBER COONEY: I agree. PCAOB should play a leadership role, and they are in a unique position to work on this. In terms of firm level AQIs, I think if the board came up with a short list and mandated that at some point relatively soon that would probably be feasible.

In terms of engagement level AQIs, I was in group three. I think I was -- I don't know if I was conservative but maybe somewhere in the middle of Sir David's pendulum.

I think they may be valuable, but my personal view is that audit committees and auditors should work together with the indicators and develop possible AQIs that at some point in future, and I was on the longer end of a possible phasing period, perhaps they should be published. But time would tell whether that was appropriate.

MR. BAUMANN: Greg, did you have a comment you wanted to make?

BOARD MEMBER THELEN: Thanks.

You know, I agree with the comments before. I think rationalizing the number certainly makes a lot of sense to make it more manageable. I like the idea of a framework.
I think that audit committees and companies and firms can work real well within the concept of a framework. So I would encourage moving that direction. And also bias towards action -- you know, we have been talking about this for a long time.

You know, if we can get some things decided and get a few of them out there let's, you know, get it out there, design and experiment something, test it out and see what we get. But let's not talk about it for three more years.

MR. BAUMANN: Joan Amble.

MEMBER AMBLE: Yes. I would favor it not being mandated. As was stated out of our group, I think a principles-based model, which talks about objectives is helpful, citing examples empowering the audit committee to engage with management and the auditors and then they would determine, the audit committee, which are most relevant and are decision useful.

I think it's -- I would emphasize in any principle-based model that one of the most important elements would be a trend analysis and, to the extent applicable, what was planned on an AQI and what the actual result was and a very substantial emphasis on the
qualitative discussions.

I would not support at this point disclosure of that. I think it's way too soon, and I would say we should walk before we run. And I think if you empower the audit committees to be thoughtful about this, you'll get a much better result and a much happier result at the end that could be very constructive and productive.

MR. JONAS: Joan, just to clarify, what, then, is the role of the regulator in a voluntary regime, in your view? What do we do here in the next year or two if anything?

MEMBER AMBLE: Actually, I don't know if you realize this, but I think you've also already provided value because you've got people thinking about it. Maybe not everybody, but you've got people thinking about it.

You have people talking about piloting it or piloting it, and I think what -- and I will get to your exact question. The other thing which I forgot to mention is a lot of these AQIs are formalizing what's already happening anyway.

You know, it's capturing, on a formal basis, data that was addressed and understood through discussions
because audit committees do stuff before the AQIs were a concept.

    I think the regulators, what they could do, is provide a really good principles-based document of this is what we would like -- this is what we encourage and these are the objectives that we think could be very, very helpful.

    I think maybe even reaching out to some people that have piloted it and said which ones work and which don't, I think trying to convey a message that 28 is the right number -- I know when we did it, we had 12 and there was -- it was more than 12 pages because there was a lot of discussion, et cetera.

    That was too many. And once you make it a burden, you've lost the benefit and, like I said, there's a lot more -- the other thing which we don't want to lose sight of is -- and this is part of the resistance, and I talked about this in our meeting -- it's a misnomer to call us an audit committee, because we don't audit.

    Okay. We don't audit, and we do a lot more things and people don't like it that we're only focusing on this, because there's a lot more that we have to do to do a good
MEMBER GALLAGHER: But you are a committee?

MR. BAUMANN: Thank you.

MEMBER AMBLE: We are a committee.

MR. BAUMANN: Mike Gallagher.

MEMBER GALLAGHER: Thanks.

I was also going to say something original until Joan just answered Greg's question, but I'm going to say it anyway.

The PCAOB and Greg, in particular, need to be commended for taking on this project, and I think that the behaviors have changed already. A number of the firms have piloted audit quality indicators and are having really good dialogues with audit committees today.

In addition to that, I think that this dialogue that was spurred by the PCAOB has caused, you know, some of the firms to speak more publicly and actually put metrics into our overall, you know, whether you call them quality reports or transparency reports -- put metrics in these reports and, you know, being one of these firms I would tell you that, you know, we struggled with how to do it, and we finally said you know what, let's just do
it. It's not going to be perfect this year.

We did it a couple years ago, and each year we're adding more indicators. So I think that the project is getting momentum, and I think the momentum was spurred by this project, and I think it's -- you know, let's let it get some more momentum and let's let -- hopefully a race to the top in terms of what firms do and what firms disclose.

MR. BAUMANN: Sandy, what do you think the PCAOB should do next?

MEMBER PETERS: Well, I think I was in the room from Venus, but I was from Mars. But I don't think --- I'm probably maybe the only investor which would say I don't think that these are ready to be disclosed right now.

I worry about them, and it may be because of the fact that I was an audit partner, that they may create a behavioral response that isn't what we as investors actually want.

And I think they may at times tell you more about the company than they do about the auditor and their underlying people, process and technology. But that's just my view.
As far as proceeding, I think that focusing on a core set of indicators is a good idea. I think that mandatory is sort of a strong word but I think that it is necessary to have audit committees have conversations around these and for the regulator to understand what that looks like, what the -- what the numbers are turning out to be, what they actually tell us, are they really measuring audit quality. So I think that there's some bias to do something. I just wouldn't -- I just would be very fearful of publishing them today, because I think they -- we really need to know what they tell us, and I think qualitative as well as quantitative are super important to the conversation.

MR. BAUMANN: Phil.

MEMBER SANTARELLI: Thank you.

I would echo Mike's comments about congratulations to Greg and his team and the PCAOB on raising the dialogue related to audit quality indicators.

I think it's been quite dramatic and, by increasing the dialogue, I think that has had an effect on audit quality in a positive way.

As far as a path forward, I don't see the need for
any specific rule-making or standard setting related to audit quality indicators.

I think the role of the regulator here is to continue to encourage a dialogue between audit committees and their auditors, certainly through your audit committee dialogue publications and so forth, and offering the concept paper as a source of data points that audit committees might consider in those conversations.

Beyond that, I'm strongly supportive of the PCAOB considering the development of a framework for audit quality. I think that would be very useful for both audit committees and auditors to adjust accordingly, and I would encourage a sense of urgency around the agenda item for upgrading and modernizing the quality control standard.

Thanks.

MR. BAUMANN: All right. Thanks. Joyce Joseph.

MEMBER JOSEPH: Thanks, Marty.

Well, as I mentioned earlier today, I do believe a principles-based framework is an appropriate approach, allowing the audit committee process to play out in using the AQIs and the data that is derived from those learnings should be used in order to make later assessments as to
what are the most plausible AQIs that could potentially be publicly made for investor consumption and, again, with direct investor input as to what would make sense for that slate of AQIs.

And I think that core set should have some degree of being mandated simply because investors do like to have benchmarks for peer comparisons and period over period comparisons.

And so it will perhaps be more informative if at that later point in time post-evaluation of the quality benefits -- that they can use it. So it's very similar to the remarks that Sandy has also made on this topic.

MR. BAUMANN: I was going to give the observers an option to pass unless you wanted to speak.

Walt Conn.

MEMBER CONN: Yeah. One of the specific ideas that was discussed in group one that, I think, was along the lines of a principles-based framework was for the PCAOB to issue a thought leadership piece that would encourage auditors and audit committees to have a dialogue about AQIs, would or could provide some example AQIs and how they should be calculated and then that thought leadership
piece could be updated after a year to discuss experiences that you hear from audit committees, from auditors, et cetera, and I think that will just build upon what the PCAOB has already done, and it struck me that that was very consistent with some of the recommendations from the group two discussion and with Bob Hirth's idea for an audit committee dialogue piece. So that would be my recommendation to pursue.

MR. BAUMANN: Guy Jubb.

MEMBER JUBB: My personal advice to the board is that it proceed with reasonable haste to require engagement auditors to discuss and agree annually with the audit committee its principles-based approach to determining and evaluating engagement audit quality and document the same. And this should be documented in appropriate detail.

Second, I would advise the board to urge the SEC to require meaningful disclosure, discussion and analysis, not boilerplate and possibly by reference to a framework, disclosure by the audit committee of its approach to evaluating the effectiveness and the quality of the audit.
In both those aspects of advice I implicitly do not encourage specific reference to the identified quality indicators as such but rather a framework approach.

And finally, that the -- my advice would be that they let this approach bed down over, say, a period of three years but infuse, in particular in relation to the audit committee engagement the board undertakes, infuse the encouragement to -- and guidance to take this forward in a meaningful way.

MR. BAUMANN: Thanks, Guy.

Jeremy Perler.

MEMBER PERLER: Thanks, Marty.

Just coming from the investor perspective, I'm a really big fan of disclosure, and I think you'd be hard pressed to find an investor who's not.

But I just don't see this information as decision useful at all from an investment perspective. I'm not a fan of quantitative metrics and especially ones that are designed to capture an inherently nuanced and qualitative system and especially ones that reach broadly across industries and geographies, because, inevitably, they get boiled down to the lowest common denominator of stuff
that's just not interpretable and, more importantly, Goodhart's law kicks in, which makes these measures -- when you establish a measure it seeks to become a useful measure, because it influences the system itself, and I think, you know, setting these up would run the risk of the engagements being structured in such a way around these metrics.

And, you know, perhaps it's helpful for an audit - from an audit committee's perspective, and I've listened to a lot of comments and interested to hear, and that's less my knowledge base, but if I were to see these from an investment perspective, I wouldn't see them as helpful at all.

So my recommendation is not -- from an investment perspective, I wouldn't move forward on that side and whatever on the audit committee's side. If it's helpful to them, great. If not, I'd kill it.

MR. BAUMANN: John White.

MEMBER WHITE: I'm probably pretty predictable on this one, but I think you should start by focusing on getting information to audit committees, and I think that information should be engagement level information, not
firm level information, with the focus being to help the audit committee members oversee their own audit, trying to figure out the kinds of information really being decision useful information with respect to, as I say, overseeing their audit, the goal being to get audit committee buy-in to the project.

I guess I would focus also -- that you have a tool out there already, this audit committee dialogue tool as a way of communicating information.

MR. BAUMANN: Thanks, John.

Tom Selleck.

MEMBER SELLING: Did you just say Tom Selleck?

MR. BAUMANN: May have sounded that way.

MEMBER SELLING: I don't know. I think I'm -- never mind, never mind. I was originally skeptical about --

MR. BAUMANN: Does that mean I didn't call you then? It's a --

MEMBER SELLING: I'm having cataract surgery soon, but I need ear surgery also.

I was originally skeptical about this project, but I know think it's extremely important. Even the best
intentioned and most highly motivated audit team is not sufficient to ensure a high-quality audit. Competence and resources are key and investors are entitled to have information about that.

I'm very pleased with the consensuses that came out of our group, and I have very little to add to Jane's summary. I think it was excellent. I encourage the PCAOB to marshal the impressive academic minds it has placed at its disposal to produce an evidence-based foundation for any guidance that it will issue.

And I do agree with Sandy and Jeremy that the question of the response by issuers and auditors to the new requirements is extremely important.

I think it is certain that there will be a behavioral effect. But I think that research and good thinking can maximize the possibility that the response by the issuer community will be a positive one.

MR. BAUMANN: Richard.

MEMBER ROEDEL: It's hard to follow Tom Selleck, but I'll try.

MEMBER SELLING: The mustache. You've got the mustache.
MEMBER ROEDEL:  Sorry. And at the risk of piling on, I'm going to start by saying I do, like a lot of people have mentioned, think that this was a project very much worth the time and the energy from the PCAOB and thanks to Greg Jonas as well, I think it is both highly relevant and as many people have said already I think it is added to the discourse about a very, very important subject.

I would encourage the board to do two things, to, first, in the short term --- and remember this is a journey, and we're certainly in the very early innings of this -- just like other disclosures required of registrants, all of us can go back in time and look at the first MD&As and the first CD&As that came out.

I think that with time and attention on the part of the PCAOB, the audit firms, and the audit committees, this process will get better with age. I would mandate a short, highly relevant, highly correlated group of AQIs to be published by the firms. But as I said earlier, to me the most important thing is to, at the end of the day, whether it's now or later, to wind up with a required communication by the firms.

And remember, there are so many firms that are --
that audit registrants that are not represented in this room that I think we need to hear from -- investors and consumers, audit committees.

I would mandate that communication, which now takes the form of a transparency report, be proscriptive about its content, and I think that that will be of enormous use to investors and to audit committees in particular who have the responsibility to making sure that not only the people who were doing that audit are qualified in however you describe that but are doing work in an environment which is conducive to audit quality at the highest level. Thank you.

MR. BAUMANN: Thank you. Elizabeth Mooney.

MEMBER MOONEY: Thanks. I do applaud your team, Greg for all the good work on this project. I do think it's important, and we have a, you know, a very extensive, robust, in-house process and effort around proxy voting, and I know this -- I believe this information really would be useful.

We do, you know, extensive fundamental analysis of the financial statements, and it would really help inform our discussions and our decisions especially from that
perspective. So I would also urge the mandatory
disclosure in the proxy filings.

MR. BAUMANN: Thanks.

Peter Clapman.

MEMBER CLAPMAN: Apart from applauding the PCAOB,
as everybody else is going to do and has done, my
recommendation is to move quickly to implement the process
of AQIs basically to recognize that the primary focus of
it, certainly at the beginning, is between the audit
committee and the audit firm, and I would permit a lot of
flexibility in terms of exactly what factors are involved
in those discussions.

But I believe the process of doing something in
this area in that engagement between the audit firm the
audit committee ought to begin right away.

Ultimately, I think investor disclosure has got to
get into this process. We've had other situations where
some disclosure, and I think the disclosure should be
around what is happening in terms of the audit firm and
the audit committee reviewing the AQIs that seem to make
sense for that particular company and that particular
industry, to have some disclosure along those lines.
Since this is the PCAOB, I would prefer the PCAOB to do it in the auditor report. If the SEC wants to take it over and put it in the proxy statement, I don't have any objection to that.

But too often we wind up in a situation where there's a question of which agency should mandate a particular disclosure, and I think investors need this and investors need to know that a process along AQI is happening, and I think the point earlier that this gives real meaning to the role of investors finally to ratify the selection of the audit firm, they need this information, so I would encourage the PCAOB to get started with it right away and to have some kind of disclosure that the process is occurring.

MR. BAUMANN: Thanks. Brandon Rees.

MR. CROTEAU: Sorry. Just --

MR. BAUMANN: I was going to give you the opportunity to pa --

MR. CROTEAU: And I appreciate that, but I'll take the opportunity this time and really, I just wanted to recognize the project team here.

I think what Greg, Steve and others are doing --
George and others are doing is incredibly useful here, very transparent in terms of developing the AQIs, and while there's a range of views around the table, I think the transparency that they've really afforded this project has enabled the SAG to really provide some very useful feedback here. And so I just wanted to take a moment to recognize them.

MR. BAUMANN: Thanks. Brandon Rees.

MEMBER REES: Thank you.

So, if the breakout session of investors was on Venus, then I'm living on the surface of the sun.

My view is that the problem with voluntary disclosures is that only those issuers that have high quality audit committees and high quality audits will be -- will really benefit from that, and it's the low -- it’s the companies that have problems that will benefit the most from having mandatory AQI -- an AQI at firm level and engagement level disclosures.

I would like to see the PCAOB move forward as the specialized agency to identify those AQIs and to require disclosure in an audit committee -- I'm sorry, in the auditor's report and then the SEC could supplement it by
requiring an audit committee discussion of the AQIs, but, at the end of the day, AQIs are the auditor's information and my view is it is most appropriate to appear in the auditor's report and I -- I guess I would just close that if -- you know, if AQIs are not measured, then they won't be managed, and, in my view, sunlight is the best disinfectant and that by disclosing AQIs, you will help those companies that are most in need of improving the quality of their audits.

MR. BAUMANN: Sir David.

MEMBER TWEEDIE: I would echo what Brandon has just said. I think this is a stewardship issue. I think it's very difficult to argue against showing the skill, competence, and experience of an audit team.

I think it will put pressure on teams that are weak to come up to scratch for the reasons Brandon gave.

I would mandate in the audit -- with the auditor reporting it, the ones that we talked about earlier, the four, and you can have qualitative things later on, and it'll just build, I think, like the MD&A did, and that's the way I'd go forward.

As far as the audit committee is concerned, I think
the first dozen or so of these indicators are useful to
them. They can always ask for more if they wish it.

I would have some sort of a dialogue with the audit
committees, but I would act now and mandate for the audit
report, the one who's dealing with the makeup, and
competence of the team.

MR. BAUMANN: Jim Cox.

MEMBER COX: First of all, I wanted to just
associate myself. I thought Guy had a great three-prong
approach and I think that's right and I want to just address
a couple of issues.

One is about whether it's mandated -- whether it's
an appropriate time to mandate anything, and I want to
point out the fact that, whether you're going to mandate
something or not, depends on what the objective of a
mandated disclosure would be.

My way of thinking about this is to the audit
committee and to the audit firms themselves. But
disclosing it to investors provides an additional impetus
for that.

Now, whether you mandate it or not mandate depends
on what you're going to mandate, okay? And so we've heard
several reports that the genie's already out of the bottle.

A lot of developments are going on. A lot of buy-in from the Big Four firms and other firms with respect to audit quality indicators.

If that's the case, then it seems appropriate that, minimally, you can have a kind of disclosure much like we've seen the SEC do early on in its governance things. For example, do -- does the audit committee employ audit quality indicators.

If not, why not? If so, what are they? Okay? You know, that would be something. It would actually serve a very useful purpose on exactly the same lines you were talking about over there of getting things out in the atmosphere so people can then learn from others.

And then if you follow disclosure, which is a history of disclosure, of it being iterative and hopefully sensible, which is not always the case -- admit that -- but an iterative process, then I think that would be a very useful process.

So yes, mandated, general at first, perhaps not quantitative, but just simply asking the question what are you doing. And by doing that, you'll get a dialogue going
which, I think, is going to point things in the right
direction.

MR. BAUMANN: Thanks. Sara.

MEMBER LEWIS: So just echoing my comments
earlier, again, this is from an audit committee
perspective.

I do think that the qualitative discussions
between audit committees, the audit firms and, you know,
your engagement partners and your management team is the
most indicative of a quality audit from the
engagement-level perspective.

But I do think that the thought leadership piece
on the audit quality indicators that we deem most important
would be very useful to audit committees and, you know,
keeping in mind that we do already receive -- I think you
mentioned numbers one, five, six, and seven -- we already
do receive and discuss those indicators on a very regular
basis as well as several others on the list.

So, you know, continuing to have those
conversations through the audit committee dialogue and our
thought leadership piece, I think, would be very useful
for audit committees.
But I do think, you know, one area where the PCAOB is in a very unique position is if over time, you know, through your inspection process, you can find an evidence-based causation between some audit, you know, audit quality indicators and things that actually do result in a very high quality audit, you know, if those are causation, not just correlation but causation that would be very useful, again, in another audit committee dialogue piece, because those things, in theory, would evolve over time and if you, again, with your root cause of failed audit, you know, work that you're doing I think that also could be very useful. And so those are the areas where I think the PCAOB can be very helpful to audit committees.

MR. BAUMANN: We've been saying that these projects are linked --- the root cause and the AQI project and the quality control standards we want to get working on.

All right. Greg Platt.

MEMBER PLATT: Yes. I would like to first add my voice to those who have congratulated Greg and his team, and I think Jane did an excellent job of summarizing the
work done in the third group.

I fall on the side of identifying a handful of universal metrics that would be immediately mandated for all issuers.

I would require adoption over the earliest practical time. I would also permit and encourage companies to report on and explain how the AQIs used actually improved and enhanced audit quality.

I also believe that a framework for developing audit quality indicators is necessary, and I believe that the PCAOB is uniquely positioned to facilitate that.

Thank you.

MR. BAUMANN: Thanks.

Maureen McNichols.

MEMBER MCNICHOLS: I think it's a great project. I think it can have very positive impact and better information for investors and potentially better incentives for audit committees and their auditors.

In terms of proceeding, I think the next step would be to start a process that ultimately leads to mandatory disclosure of some AQIs. So which ones?

Well, in terms of the metrics in Attachment B, the
28 metrics, many of the audit results-related metrics are actually already public.

So from the investor standpoint, and, actually, investors do find those informative. We have data on that, evidence on that.

So, I think from an investor standpoint the greatest potential benefit is going to come from things that aren't already being publicly disclosed, and I support the recommendations Sir David made in terms of focusing on understanding better the qualities of the audit team.

So I would recommend a phase one that develops the AQIs in the phase one the audit professionals category in Attachment B taking an evidence-based approach and say relating it to the evidence and inspections to document why these would be relevant and proceeding to establish that they would be informative.

MR. BAUMANN: Thanks. Doug Maine.

MEMBER MAINE: I am a member of three public company audit committees. There are ten individuals in total. We are former CEOs, CFOs, Wall Streeters, and two generals.
None of us have ever worked in public accounting. None of us have ever managed an audit engagement team. So I view these as not only helpful, but I view them as necessary.

My one plea would be let's get on with it. Don't study it to death. Let's get something out. I'm not hung up in what form or how they're communicated. Let's just get them out.

And the last point I want to make to the PCAOB is that Jeanette was in -- I was in group one, and she was in group one as well, and she gave us her vision, and I would say that resonated very well with all the members of group one. So my advice is listen to Jeanette.

MR. BAUMANN: That sounds good. That's a decision then. We'll have to hear that for the entire group, Jeanette. So --

MEMBER HAMBLEN: I want to thank the other Jane for an excellent summary of what we discussed in group three. I would just highlight my agreement that we should move forward, that the PCAOB should move forward with mandatory disclosure of a limited number of AQIs, and that those AQIs should relate to, as others have discussed, the
experience, the expertise and the availability of the audit team and that it's -- would also be very helpful for the PCAOB to establish definitions of the AQIs that will be reported so that there's consistency and comparability.

You know, in my experience representing an institutional investor, it is important to be able to evaluate the quality of the audit and whether the audit committee itself is doing its job and this information would be a step toward enabling the investor to do that.


MEMBER PLATT:  Well first, I'd like to, as many people around the table have already done, congratulate Greg and his team on, really, an unprecedented level of transparency and a number of firsts as his project has evolved.

I mean, his -- the openness, and the discussion, and the dialogue including at the SAG meetings has been extremely valuable, especially in an area that is new to all of us.

And among the first, though I don't think it's been mentioned at this meeting, and I don't know -- I don't know how many people in this room have actually clicked on the
PCAOB website and looked -- listened to, I guess, the first podcast that they have in the series, which Greg actually has an excellent podcast on audit quality indicators from the perspective of an audit committee chair. So if you haven't done that, I'd encourage you to do it. It's certainly a good -- it's well worth the time you would spend listening to it.

This is an area where I still believe that we can and should, at this point, in the project create demand, and let demand pull from an audit committee perspective. I think many people around the room who are audit committee members or chairs have, once they learn about audit quality indicators, are wanting to embrace them, wanting to incorporate them and in the way they work with their auditor, manage the audit relationship.

And I think the continued outreach that the PCAOB has, whether it's through audit committee dialogues or speaking on panels or at events of the, you know, NACD or other opportunities for directors, things like the podcast are ways that I think we can create demand that will encourage and drive incorporation at the audit committee level.
I don't think we need regulation right now, and I think we should let, in essence, the activities you engage in drive that. Another thing that came to mind that, as an opportunity to engage individually with audit committees, as I know your inspection team, at times, do talk to audit committee chairs. It would be an interesting question for a PCAOB inspector to ask about what that audit committee chair's either experiences with audit quality indicators or whether they thought about him or whether they've engaged in discussions, just another way to, you know, maybe plant the seeds for demand in this area.

I've listened very carefully to the group three in terms of reporting to investors, and I've listened very carefully because it is -- it's not the conclusion I would come to.

I don't think we're ready for disclosure to investors, and I've tried to be open minded as I listened to the proponents of having a limited list of reporting to investors and while a limited list takes away some of the fear and uncertainty I would have, I still worry about the unintended consequences of it.
I do think that if we're going to have reporting to investors, I do think it's very important to have either the correlation or causation done, and I worry that, in essence, what we do is we drive everybody to an average in those five indicators, and we end up doing more harm than good to audit quality on the population at large.

MR. BAUMANN: Thanks.

Sydney Garmong.

MEMBER GARMONG: Yeah, I too would like to -- I thank the PCAOB for starting the dialogue, and there really is the opportunity to have a meaningful impact just from starting that dialogue.

We obviously have varying views around the table and I would ask the PCAOB to be particularly mindful when thinking about the implications for the middle market smaller filers.

I think that you're looking at a very different investor base. I think you're looking at -- well, somebody already made the comment that not all audit committees are created equal, and I think that I would encourage the PCAOB to keep that in mind.

In terms of -- in terms of moving forward with
something mandatory, I do get concerned that we might be introducing a lot of cost and effort into the system when maybe it's just not going to be valued by everybody.

So what should the board do? I think the board should continue the dialogue and, encourage, I think, just by -- I think, Bill, maybe you made the comment about well, guys just -- once they learn about it, there just becomes demand. And so I think encouraging dialogue with audit committees and investors would be -- would be very useful.

The other thing that came to mind for me is, and I know transparency reporting has been mentioned a couple of times, maybe the PCAOB would reach out to the firms and try to understand just how are people using the transparency report.

So, maybe that's something that could be done during the inspection process.

MR. BAUMANN: Thanks, Sydney.

MEMBER HIRTH: Okay. I like, Bill, your idea of this create demand program. So I think the speeches, whether it's through the audit committee dialogue or whatever just get the message out, and I'd just encourage maybe to go one step further and kind of think about it
from a marketing perspective and spend a little bit more
time thinking about the NACD and the organizations I
mentioned to get that out there. So the demand kind of
-- create demand gets exponentialized around that.

And then yeah, continue the research and the
considerations and the project itself that Greg and others
are running and consider all the comments that are here
today and then, you know, I think, to some extent, if you
can find them, watch what happens and identify the leaders
and the laggards and learn from that.

But here's something that's new that we haven't
talked about. So, if the goal of AQIs is to improve audit
quality, and if evidence of a lack of audit quality are
the deficiencies in the inspection reports, and I know
you're working on this root cause, so really tie that, and
the idea would be as AQIs go up, deficiencies would go down.

And I think you have a very interesting opportunity
here now, as the regulator, in the inspection process not
saying that any of this would be reported in the future
inspection reports but when you now do an inspection why
don't you collect certain quantitative AQIs as part of the
inspection process? So let me give you the example.
You now take a U.S. LLP, and there are 56 audits that are inspected. You ask for x AQIs that are quantitative for the 56 inspected audits. Now what you watch is you see is there any correlation.

So I've done the 56 inspections. I have these deficiencies around ICFR, around IPE, around this and that, and then look at the AQI information, and you might say there is no correlation.

But interestingly, where we had these eight same deficiencies, they came from engagements that this was the AQI amount or measurement. So I think there's an opportunity to sort of pilot that a little bit stealthily, keep the dialogue going to get that.

But I think you got this great lab opportunity, especially around the quantitative stuff, to do that as you inspect the firms.

MR. BAUMANN: That's an excellent point. Certainly, our inspectors have this kind of information available at their fingertips and look at these types of -- who's on the team, leverage and all those kinds of things, and they are tying that in with root cause, but it's a great recommendation.
Thanks. Jeff Tate.

MEMBER TATE: Great. Thank you.

A couple of comments here that I'll just make as I'm very happy to hear some of the comments that are made around not necessarily making a mandate synonymous with action.

I think you can get a lot of the actions from a thought leadership piece. I think we've got a great foundation of data and information here, and I'd love to see the project team continue to look at the tangible benefits that this can derive for the key stakeholders.

In my opinion, the key stakeholders are obviously the audit committee, the firms, and the investors when you talk about the AQIs.

So looking at the tangible benefits, also looking at the potential behaviors that this will drive for those stakeholders as you go through the project.

And then coming up with some of those key, as we've talked about before, AQIs that we can really use and find valuable while at the end of the day also assessing what's currently being done from a qualitative perspective between the firms and the audit committees and how this
could complement that.

I think that builds a lot of credibility with all
of those that we have been focusing on here as we look at
the project outcome.

MR. BAUMANN: Great.

David Kane.

MEMBER KANE: Yeah, Marty. I will break it down
into three parts. For me, it feels like a lot of has been
accomplished in a very short period of time.

So the PCAOB wants to continue to encourage and
foster communications and discussions between audit
committees and auditors on that.

Second is really monitor what those discussions
look like -- what are the factors that were specifically
considered and why, which AQIs, what's the context needed
in order to understand those and then really use that to
get smarter around and more educated around what the real
next steps should be.

I don't think we're at a point right now where that
should be mandated. I think that could be potentially
down the road as we collectively get better and smarter
around some of this, and I think the challenge is, again,
a lot of credit goes to the board and Greg and team on this. How do you keep the momentum going, but not stifle the innovation around this? So I just caution you to think about that.

MR. BAUMANN: Thank you.

Charles Elson.

MEMBER ELSON: It's always good going fortieth. You learn a lot.

A couple things. Number one, I think the notion of the AQI is actually a pretty good one for a lot of reasons. I do think that you have too many categories, because I think the more categories you have, the less focused you become on the whole project.

So I would concur with the earlier comments that it's probably better to have fewer than the 20 some odd you've got now.

That being said, the question is what is the value of this thing, and I think that any time you force someone to be introspective and review what they're doing, that's, to me, the real value of it.

The fact that a firm has to think about these things in reviewing an audit I think is the value. Vis-à-vis
making disclosure mandatory, I would be against that simply because I think when you create mandatory disclosure, the whole exercise ends up as legal boilerplate and you lose a lot of the effectiveness of it. People, you know, do the disclosure to meet the legal requirement as opposed to thinking about what went behind the project to begin with, and I would keep it voluntary because, I think you'll ultimately get better audits out of it as opposed to a mandatory requirement.

Now, the bigger question, though, and I think the end question is does this really mean anything to audit committees and to investors? And I think any transparency is always good, and it's frankly good to have it. The more information an investor has, or committee, the better they'll be.

The question, though is, and this is probably a little more on the controversial side, ratings are only helpful if you have a real choice in who you can pick. In other words, you know, higher ratings, lower ratings suggest a competitive market place.

And, you know, at this point, in the large CAP companies, there really isn't all that much choice.
You're really down to, you know, a couple of firms and with conflicts and what not that makes it a lot tougher. So I think ultimately the bigger question is, you know, competitiveness and choice, if you will, for committees the ratings only really matter if you can really -- if you really have a choice, and I think choices today are much more limited than they used to be and something to think about.

That's why you have a couple of us academics here. We're supposed to, you know, throw in the -- throw in the controversial stuff. But that I do think it's a great project, and I think very thoughtfully done and eager to see it to its conclusion.

MR. BAUMANN: The value of that academic thinking. Next, Mike Santay, you have as an observer the option to comment.

MR. SANTAY: Just a couple things. I do -- have observed that I think it would be difficult to have a broad impact without mandating some type of discussion, and I think that the ideas out of group three, principles-based with some themes might be helpful.

I do take, I think, Sydney's point about being
cautious with the impact on the smaller and mid-size firms and watching the administrative burden that this might join. I do think that their level of engagement might improve, but I don't think we want this to be a huge burden for those firms.

MR. BAUMANN: Thank you. Sri?

MEMBER RAMAMOORTI: I would also like to applaud Greg and his team for their diligence and focus. But let me also take this opportunity to appreciate Marty and his team for this SAG meeting to have these breakout sessions that has brought us to this juncture this morning.

I think this is probably the best input that we could have gotten, and that's because of the process by which we've arrived at this point. So let me put that on record.

I particularly appreciate Brandon and Sir David for their cogent arguments and influencing me this morning in supporting a bias for action.

So I would suggest that the PCAOB move ahead. And quoting Victor Hugo, audit quality is an idea whose time has come, and many audit committees in the past perhaps have been guilty of picking auditors based on cost rather...
than audit quality.

So audit quality does need to become a topic of conversation between auditors and audit committees.

I would say that a principle-based approach to the extent possible, you know, should be adopted and then seriously considered. Additional guidance should be provided for the inexpert user community among the investors as well as, you know, audit committees that may not be, you know, really ideal for this.

I also want to observe the PCAOB is uniquely in that leadership position to become the tide that lifts all boats and improve audit quality worldwide by doing something like this. This is an effect that will echo around capital markets around the world. Not just here. And that's the influence that the PCAOB can have with this kind of a project. So that is something to be considered, too.

And, in that spirit, and continuing the quoting penchant that I have, I shall quote G.K. Chesterton, who did say today's heresy is tomorrow's orthodoxy.

MR. BAUMANN: Well said. Thank you.

Chuck Senatore.

MEMBER SENATORE: I see Jeanette's to my right.
But I was hoping for the opportunity to listen to Jeanette, but I guess I'll have to wait for that.

I think we're in a situation where we're thinking about two things. One, how to empower an audit committee and, again, sort of talking about what we talked about earlier, all audit committees aren't created equal and we really want to empower and give the tools to audit committees to engage -- have great audit engagements and benefit investors.

So this needs to be driven towards that end. So the question is, in terms of the role of the regulator, do you mandate, or do you sort of let the marketplace take its course and have some different level of engagement from the PCAOB.

It's my own view that, sometimes, regulation can tend to be a blunt instrument. I've had experience with it on both sides of the table, and what I get concerned about is it can actually stifle innovation and, sort of, have unintended consequences such as, sort of, check the box kind of outcomes and some of the points raised earlier, sort of, doing it just because the rule requires it as opposed to actually trying to deal with what the outcome
should be. So that being said, so what does the PCAOB do about this?

First, I very much like what Sir David said in terms of the importance of narrowing. Although I wouldn't mandate it, I would not underestimate the power of the bully pulpit.

I think we see some examples where, when you consider the -- sort of, the incentives that exist today in audit committees, they are not without liability. They certainly have enough self-interest to make sure that they're doing their jobs well.

They recognize their duties, and the pain and the consequences for not doing them well is a very, very great incentive to, sort of, having the bar be raised. So that being said, I think that if they were to hear from the PCAOB pretty much along the lines of what the SEC has done with its risk alerts, people listen to it.

People drive behaviors toward it. People actually make changes based upon them, and they're very, very conscious of them.

So what I would do is, sort of, borrow from the Bob Hirth idea in terms of really thinking more directly and,
frankly, putting a thumb on the scale in terms of stating
the views of the PCAOB, using the PCAOB's point of view
in terms of seeing the landscape in terms of suggesting
and giving thoughts about audit quality indicators, and,
sort of, going down that road.

I suspect because of the incentives that are there
that there will be a race to the top. However, if there
is not a race to the top, the mandatory regulatory card
is always available to be played.

A separate point is something that Jim Cox said.
Actually, I made a note on this when I was reviewing the
materials -- I think, although it's sort of outside the
scope of the PCAOB, that considering in order to, sort of,
have a issuer-based kind of incentive here, have an audit
committee or an issuer disclose whether or not they use
audit quality indicators is a very, very interesting thing
to think about in terms of driving behaviors to having
better audits.

So net -- net, I wouldn't mandate. I would
shamelessly and aggressively use the bully pulpit and see
how it goes.

MR. BAUMANN: Thank you.
Megan, option to comment or not?

MS. ZIETSMAN: Thanks, Marty. Just real brief. I think that some tremendous work has been done by Greg and his team in really highlighting issues and moving this on and I think I would encourage the team to listen to some really good ideas that have been put forward around the table around developing a framework, pushing forward, using all the vehicles available to the PCAOB to really publicize this, draw attention to this and I think like Chuck just said people do pay attention to what the PCAOB says in whatever form.

So I think that there's a lot of pay to be done in terms of looking at things like the audit committee dialogues, like the podcast that Bill mentioned to really keep this alive.

But always a caution around being overly prescriptive and too many rules because that will stifle the innovative thinking and I think this will need to continue to evolve and the danger really is that if you try to box it in the unintended consequences or the - I think it will build negativity rather than a real positive atmosphere that is around it today.
So I think there's some tremendous work being done and really scoped to take it to the next level.

MR. BAUMANN: Thanks, Megan.

Larry, option to comment?

MR. SMITH: So when I look at the list of AQIs I basically divide them into two buckets - those related to the firm and those related to engagements.

And quite frankly, the firm wide AQIs I think are part and parcel of your inspection process and should guide you in your inspections and you already gather a lot of that kind of data. So I would stop talking about that with the SAG and just have that be part of your inspection process.

In terms of the firm wide or the engagement wide, I am extremely fearful that to mandate et cetera would have unintended consequences that aren't necessarily the best consequences.

I think from an engagement level perspective, context is the most important thing that's needed in order to understand the particular responses to quality indicators and I think if we were to require disclosure of those it could lead firms to make not the best decisions.
in order to come up with certain metrics.

So an example of that would be if you believe that the amount of experience in a particular industry is important but you have two audit partners or audit people being considered for an engagement, one of which as a decent amount of experience in that industry, another of which doesn't but yet has proven themselves to be very adept at leading audit teams and finding things out, et cetera, the firm might select the lesser of the two qualified candidates but yet in communications with an audit committee they can explain why that person might be more appropriate. So I'm really fearful of that.

So therefore, I really think that this should be a voluntary type of an endeavor by the PCAOB. But as a standard setter, I personally am against putting in words of encouragement in our standards because it raises really questions on the part of people as to whether it's something that needs to be followed or not be followed.

So I was curious as to exactly what your mandate was. So I went back to Sarbanes-Oxley and saw in 101(c)(5) under the duties of the board that in fact one of your functions is to, you know, to effectively foster the
improvement in audit quality. So it falls into your bucket.

But I think what you're doing in terms of developing these things and perhaps working with the SAG and working with the CAQ or others in terms of voluntarily recommending the use of these AQIs and engagement level is something that can raise the quality of audits.

But, again, I would not mandate it nor would I publish the results of them.


MEMBER JOY: Thank you.

Based on all of the discussions surrounding this over the last 18 months or so, there is such difficulty in adopting a prescriptive defined set of AQIs and there is still the fear of having them being taken out of context.

So as a result of that, I would not be in favor of a mandatory approach or making such information publicly available at this time.

However, I am very much in favor of a concept where there is some type of tool or framework that is principles-based that would foster the continued discussion with audit committees and provide further
information for their use.

I continue to look at that tool as being surrounded
on one hand by the QC standards themselves and believe that
we do need to pay particular attention to those QC
standards and based on the information that you're getting
from your inspections are those QC standards where you want
them and where you believe they need to be.

And on the other side of this framework would be
the inspection results themselves and that root cause
analysis so that we do get back to the cause and effect
of some of these audit quality indicators.

I also think if there is a framework sitting in the
middle where the standards are feeding into the framework,
the root cause analysis is feeding into the framework that
we have the principles-based framework and that also goes
to the scalability issue, that I think if it is a
principles-based framework working with smaller companies
that that is something that we would be able to deal with
in smaller companies would be able to deal with and say
what is appropriate at their level.

MR. BAUMANN: Thank you very much.

Richard Breeden.
BOARD MEMBER BREEDEN: Thank you. I would add my
voice to those others who have commended the PCAOB for
initiating this project and to the exceptional quality of
the staff work that has gone into this.

I think you have done a real service to the country
in this entire process. As a former regulator, and I
suspect former prosecutors would say the same thing, the
hardest challenge is having the courage not to act when
action is premature or inappropriate.

It is far easier when a snowball is rolling
downhill or an avalanche globally to go along than to say
no, we're not ready - this cake is not ready for prime time,

half baked. And I think that's where we are here.

This issue reminds me very much, and I think the
risks are similar, to the risk-adjusted capital rules of
the banking system. Forty to 50 years ago, bank
regulators were wrestling with the problem of bank
failures and how to prevent it even though failed audits
and bank failures will go on to the end of time no matter
what regulators do.

But it is certainly something they were worried
about and they came up with the idea well, shouldn't
capital rules be variable based on the risk of the bank.

And whether academics or people in the practical world they all said well, it's kind of hard to argue against the proposition that capital rules should vary based on the riskiness of assets, except for two problems. One, no human being and no group of human beings is capable of measuring prospectively risk and financial markets accurately.

It takes the collective judgment of millions of participants in the market to do that and so there was a built-in hubris to the exercise.

And two, even if one came up with something that was relatively close to an assessment of risk it can't take into account the fact that people will then respond to the rule and will engineer to any rule that is produced.

And so in 2008, after multiple efforts at this, bank failures in Europe were exactly inversely correlated to regulatory capital.

Those banks that had the highest level of Basel Tier One capital failed most often and those who had the lowest levels of regulatory capital did not fail.

And I worry that - I mean, I think this illustrates
the problem of a concept. It is impossible to argue that audit quality isn't important and that audit committees and investors and users in the markets don't want all the information they can get about audit quality.

But can you really regulate it and can you mandate anything that will end up not being counterproductive and I don't think it can be done.

When we wrestled with the commission in my era with things like pay ratios and disclosure - transparency about well, what's the ratio between the CEO's pay and the average worker's pay and we asked the question, well, then suppose we're going to have that ratio published for AT&T with 350,000 employees and also published for Albert Einstein & Company, which is a small IPO company consisting of Albert Einstein and one lab assistant.

And the fact of the matter is one size fits all ratios do not work well in the real world. So I believe that audit quality is an elusive and complex thing that is composed not only of the numeric indicators, which are relevant - they're just not dispositive - but also things like character of the engagement partner and character of the managers and the other participants on the audit team
and the culture of a firm, and those things don't get measured when you start coming up with quantitative indicators.

And in fact, as you've heard before, I've strongly supported the PCAOB's effort to have disclosure of the name of the engagement partner and that's because it is the character and culture and experience and history of the engagement partner that is highly relevant to the quality of a particular audit engagement and firm level AQIs are in a sense, inconsistent with that.

So forgive me for going on too long. I believe you should not mandate any AQIs. I believe you should require each registrant to publish not less than every five years or not more frequently than biannually a statement regarding what it deems to be the most relevant audit quality indicators for their firm.

And then I believe the PCAOB should publish a summary and archive this and so that it is any audit committee can easily obtain the publication of every audit firm on audit quality and if a firm chooses to have a one-sentence report that says we don't believe in audit quality so be it and then let the market decide. Thanks.

MEMBER MURRAY: We quite regularly celebrate what Greg and his staff have done on this subject but I go more broadly than that.

I personally found this meeting to have been a most satisfying - probably the most satisfying in several years I've been on SAG in a couple of respects - in a personally stimulating occasion and it has given us an opportunity as a group to begin to hear each other and I appreciate all that - the work that has gone into that by Marty, the staff and the board to help get us to this point.

To the - to the issue. My views were part of the group two consensus that Greg described so well yesterday. I won't repeat the details.

I will address the question of what should the PCAOB do now and I probably - this is a superficial version of the Richard Breeden school of advice.

The PCAOB should declare victory, should remind the world that thought leadership is a valuable tool of regulation and that regulators are not limited to standard setting in what they can do and monitor for three years and see where nature takes this issue.
I have to acknowledge and thank Brandon for an observation that I think deserves a bit more attention when he reminds us of the misalignment of the planets in our particular universe.

Mars and Venus are not well aligned today, and I think the misalignment is a critical issue for quality of financial reporting and the orderliness of improvements that we all want to achieve there.

I think the biggest problem is not difference in objective but difference in perception.

The Mars community looks at auditors and audit committees and assumes that given a choice they will most of the time elect to be self-serving rather than public serving.

And the other community looks at the investor community and assumes that it's not really investment-related decision making for which they seek additional information but other investor-oriented initiatives that are not really part of the capital markets process.

I'm sure there is fault in both of those perceptions and some truth. I think reconciling to the
extent possible, sorting and filtering out the perceptions that are mistaken and can be corrected is something that SAG can be useful to in the broader community of U.S. financial reporting.

So I would urge that we find a way to communicate toward the objective of aligning the planets into a little more harmonious state than they seem to be at the moment.

Thank you.

MR. BAUMANN: Thanks, Rick.

And John, you have the final word.

MEMBER LUKOMNIK: Going last is even better than going 40th. I'd like to add my congratulations and I think it's important to note amid all the disagreements how much agreement there actually has been around the table and I'll get to that.

I'm not going to restate my opinion. That was clear before. But I do want to take the charge to us which is what should the PCAOB do now, seriously.

When I was growing up, there was a play on Broadway called "Gemini" which was about a dysfunctional family. No implications. And the teenage son used to belly up to the dining table and just grab the food and shove it in
his mouth and the mother would say, "Take human bites."

I think that's good advice for the board. We heard Chairman Breeden talk about basically firm-level disclosure.

We've spoken about engagement level disclosure - Professor Cox gave a great idea for the advisory to the SEC. I would move for unanimous approval. Unfortunately, it's not in terms of disclosure at an audit community level.

I think these are two very different sets of indicators. I do think you should bifurcate your processes as they go forward. It will result in less confusion and less controversy.

It will also enable you to focus. I also - so to what the agreement has been, I have heard no one say the industry - the public issuer community or investors do not need audit quality indicators. AQIs were not a term of art five years ago. That is a pretty amazing progress.

The boundaries of the discussion are should you mandate a small set of indicators allowing audit committees, auditors and members to disclose more of them.

No one has said mandate all 28. Or should you take
action to encourage voluntary adoption and perhaps disclosure. No one is saying prohibit disclosure. That is actually a relatively narrow range and you should be proud of the process which has gotten us all to that.

Professor Cox says towards what end do you regulate. I think the clear end here is audit quality improvement which has an intermediate step which is marketplace adoption and marketplace disclosure.

As Richard said, it is a process. I have no doubt that we will get there. I think that those of us who are arguing for mandating a small group and allowing flexibility around them versus those who are arguing don't mandate but encourage wide adoption are trying to get to the same place - perhaps through different routes at different speeds but to the same place.

And so what I would encourage is whatever you do on this, please keep up the momentum. They are not mutually exclusive.

For instance, were you to choose to mandate there is nothing that prohibits you from issuing an audit dialogue or using speeches or the bully pulpit, generally, in addition. If you didn't choose to mandate there is
nothing.

We have a great momentum on this. I don't think the range is that different. Ten years from now every audit committee, every auditor will be using AQIs. There will be disclosure to investors. However we get there, whether it is through - I mean, it's majority voting. It's proxy access. The lineage is clear. Whether it is mandated or voluntary we'll get there.

I would urge the PCAOB to bifurcating it by narrowing the focus to take a leadership position and getting us there as quickly as possible. I think the way you do that is by narrowing the conversation.

MR. JONAS: Well, to say the least, I know all of us on the project team and the board feel that we've benefitted hugely from the SAG's input in the past and I can assure you we have benefitted hugely from what has occurred here in the last two days. So we can't thank you enough.

(...)