

NOTICE: This is an unofficial transcript of the portion of the Public Company Accounting Oversight Board's Investor Advisory Group meeting on October 20, 2014 that relates to the Board's Proposed Auditing Standards on the Auditor's Report and the Auditor's Responsibilities Regarding Other Information and Related Amendments. The other topics discussed during the October 20, 2014 meeting are not included in this transcript excerpt.

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http://pcaobus.org/News/Events/Pages/10202014_IAG.aspx

PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

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INVESTOR ADVISORY GROUP

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MEETING

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MONDAY, OCTOBER 20, 2014

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The Advisory Group met in the Hamilton Ballroom of the Hamilton Crowne Plaza Hotel, 1001 Fourteenth Street, Northwest, Washington, D.C. at 9:00 a.m., Steve Harris, Chairman, presiding.

PRESENT

STEVE HARRIS, PCAOB staff, Chairman
 BRANDON BECKER, TIAA-CREF
 ROBERT T. BUETTNER, Newbrook Capital Advisors
 MERCER E. BULLARD, University of Mississippi,
 Plancorp, LLC, and Fund Democracy, Inc.
 CURTIS L. BUSER, The Carlyle Group
 T. GRANT CALLERY, formerly of FINRA
 JOSEPH V. CARCELLO, University of Tennessee
 NORMAN J. HARRISON, FTI Consulting, Inc.
 MICHAEL J. HEAD, Creighton University
 PETER H. NACHTWEY, Legg Mason, Inc.
 BARBARA L. ROPER, Consumer Federation of America
 LAWRENCE M. SHOVER, Solutions Funds Group
 DAMON A. SILVERS, AFL-CIO
 TONY SONDHI, A.C. Sondhi & Associates, LLC
 JUDGE STANLEY SPORKIN, U.S. District Court
 (Retired)
 ROBERT M. TAROLA, Right Advisory, LLC
 LYNN E. TURNER, LitiNomics
 GARY G. WALSH, Luther King Capital Management
 ANN L. YERGER, Council of Institutional Investors

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 WASHINGTON, D.C. 20005-3701

ALSO PRESENT

JIM DOTY, PCAOB Director
BRIAN CROTEAU, Securities and Exchange
Commission
MARTIN BAUMANN, PCAOB
LEWIS FERGUSON, PCAOB
JEANETTE FRANZEL, PCAOB
JAY HANSON, PCAOB
JAMES SCHNURR, Securities and Exchange
Commission
MARY JO WHITE, Securities and Exchange
Commission, Chair

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18 MEMBER YERGER: Okay. Our first but final
19 recommendation is urging an expanded audit report. I
20 could almost repeat all the comments I made about the
21 signature, this is not a new issue for the Board which
22 is -- it's been considering the issue. It's actually not

1 a new issue for this committee, we have discussed it and
2 I think supported it quite robustly. And it's not a new
3 issue globally, as we've discussed, expanded reports are
4 in place in other countries and as we've learned, I think
5 the Rolls Royce example is a terrific one, actually it
6 seems to be working in a really significant way.

7 So you know, the issue of the quality of the
8 audit report really has been debated for decades and I
9 think there is value from an investor standpoint in the
10 current very blunt pass/fail model that's in the report.
11 It's concise, it's clear, it's comparable. But I think
12 it is clear today that the current auditor's report is
13 just not satisfying the needs and interests of investors
14 who really are the final and the ultimate customer of
15 these products. As we surveyed the members of -- what
16 was it -- of the investors two and a half, maybe, two
17 years ago, three years ago, on this issue there was
18 strong support for an enhanced audit report from the
19 investor community. CFA Institute has similarly surveyed
20 its members and found the same thing. So this is a space
21 where I think investors' viewpoint is pretty consistent
22 and clear, that they would like to know more from the

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1 auditors.

2 You know, we do believe there's going to be an
3 enhancement of audit quality if the auditor's report
4 would be expanded, but I think there are also some other
5 real benefits for investors from an expanded report.
6 First of all, I view auditors as independent experts who
7 have knowledge about the company that, you know, most of
8 us investors can't get at. I think there would be real
9 value in gaining from some of their knowledge and
10 expertise and it would help investors analyze and price
11 risks and make investment decisions.

12 I think an expanded report would really heighten
13 the perceived value of the audit firm work, something
14 that Lynn discussed earlier, and I think it might give
15 firms some leverage to effect change and enhance
16 management's disclosures and practices. And I finally
17 think that this expanded reporting would enhance the
18 transparency and promote real confidence in audited
19 financials.

20 In terms of cost, Steve, you brought this up
21 earlier, I think a lot of the things that we would like
22 to see in that expanded report, sort of what was in the

1 Rolls Royce report, is probably already being
2 communicated to the audit committees, so I don't know
3 that I see this as a really expensive undertaking in
4 terms of disclosing to the public.

5 And I also note, I know that there's a lot of
6 debate about who should this expanded information be
7 coming from? Should it come from the audit committee?
8 Should it come from the outside auditor? And my view is
9 there's real value in getting the insights from the
10 outside auditor, the independent expert that's been
11 retained by the firm. I believe there could be better
12 disclosures from the audit committee but I don't think
13 that the audit committee should solely be responsible for
14 this.

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8 MEMBER SILVERS: First, my thanks to my
9 colleagues for picking up after me. I was at lunch with
10 my wife and didn't realize that I was up next. So now
11 I've gathered my thoughts, I have a couple of things to
12 say about this.

13 The first is to repeat what I guess has been --
14 actually what someone said earlier which is, in relation
15 to the question of the expanded audit report, it only --
16 just to put a further gloss on the recommendations that
17 are here, it only makes -- it's only going to work, I
18 think, if there's a requirement to disclose something.
19 Meaning that if basically the expanded audit report is
20 a mandate to tell us, tell the public, tell investors if
21 something is wrong. The audit firm will, of course, say
22 nothing is wrong.

1 Now that requirement, that further requirement
2 may give the audit firm some leverage in private
3 negotiations with the issuer but it's not going to result
4 in any new information. What will result in new
5 information is the requirement to disclose, you know, for
6 example, the most -- you know, every audit has matters
7 that come up that are of concern to the auditor that are
8 generally resolved in some fashion that's mutually
9 acceptable. The requirement to disclose the most salient
10 such matter, there's always one, right? And the notion
11 that you can't say nothing seems to me to be something
12 that would actually add value of the kind that the
13 examples in our report outline.

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MEMER CARCELLO:

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20 And then in terms of the audit report based on

21 some of the work that Ann and Norman and Gus Sauder, who

22 used to be a member of this group, did a few years ago,

1 basically what we heard from users is, although they
2 found the audit useful, they didn't even look at the
3 report because it had no information content. And there
4 are other things we could come up with but at a minimum
5 I think those three are indicative of the fact that there
6 are issues with both audits and the communication of the
7 audit results, that these recommendations are designed
8 to try to be responsive to.

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CHAIRMAN DOTY:

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12 If you start thinking of what we do in terms of
13 the disclosures that we can now implement to enhance
14 confidence that the public is getting the facts about the
15 audit, and certainly they are, the audit reporting model
16 is the biggest project going in that regard, the
17 practices in the firm that we can lobby for successfully
18 in talking to the firms. And then the final ultima ratio
19 of where we can say we think this responsibility comes
20 to rest outside, those are three fairly important sticks
21 that we have to wield. They are three fairly important
22 devices we have for improving audit quality.

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MEMBER CARCELLO:

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20 If you look at comment letters on the expansion
21 of the audit report, most, if not all of the
22 institutional investors that have commented support that.

1 Audit committees seem to be almost unanimous in their
2 opposition. So these are groups that are supposed to
3 represent the interests of investors and on major policy
4 issues are taking policy positions opposite that espoused
5 by investors.

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MR. BAUMANN:

1 So we've issued a proposal for the auditor to
2 disclose critical audit matters in the audit report and
3 also to describe what the auditor's responsibility was
4 with respect to other information accompanying the
5 financial statements. Some of the non-audited -- some
6 of the non-GAAP measures and others which could be
7 reported in the other information where the auditor has
8 to read and consider that. But we were heightening some
9 of the requirements there.

10 We also held public hearings on the expanded
11 auditor report in April of 2014. So our plan now is to
12 issue a reproposal on expanded auditor reporting
13 requirements, taking into account the comments we
14 received during the comment period as well as at the
15 public meeting and to issue that reproposal probably in
16 the first quarter of 2015. We are staying obviously very
17 close to all of those global developments and have had
18 many conversations with the IAASB and European Commission
19 and others.

20 Just in terms of timing, somebody mentioned
21 falling behind, hopefully we won't fall too far behind
22 here. the IAASB expects to approve a standard on

1 expanded auditor reporting at their December meeting.
2 And that they expect to be effective for year's ending
3 on or after December 15th, 2016 such that expanded
4 auditor reporting would take place in 2017. So if we can
5 get our reproposal out in the first quarter as I
6 suggested, and hopefully move that along, maybe we can
7 get on track.

8 By the way, that IAASB report that they expect to
9 approve in December, the IAASB report, does include a
10 requirement to disclose the name of the engagement
11 partner in the audit report so that will be a requirement
12 basically around the world for all those countries over
13 100 jurisdictions that follow international auditing
14 standards. So again, please weigh in on that reproposal
15 on expanded auditor reporting that we'll issue in the
16 first quarter of 2015.

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MEMBER NACHTWEY :

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3 And then on this expanded audit report, that we
4 get it right and that it's useful information and not
5 just a lot of boilerplate at the end of the day, if we're
6 going to have companies and the investors in those
7 companies paying for that extra work.

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1 MEMBER HARRISON:

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7 I'll be brief because first of all some of the
8 observations I would have offered have been covered
9 already. I don't want to be repetitive. I'll end on the
10 note or theme I mentioned in one of my comments earlier,
11 and that is that I would strongly urge the Board, in
12 everything you do, but in particular in the rulemaking
13 in which you engage that pertains to the audit report and
14 some of the other disclosure-oriented issues that we've
15 mentioned today, to bear in mind that one of the things
16 that the audit profession and audit firms can do where
17 I think there is tremendous room for improvement is to
18 be an additional source of valuable information that
19 informs the investment process, as we discussed earlier.

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