PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

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STANDING ADVISORY GROUP

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MEETING

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MS. RAND: Thank you, Marty. Good morning, everyone. As Marty said, we will continue our discussion on the auditor's reporting model.
Before we do that, though, I want to remind you of our disclaimer, which is the views expressed by each of the presenters are our own personal views and not necessarily those of the PCAOB, Members of the Board or other PCAOB staff.

So, getting into our discussion, yesterday we spent our time, and our time had been abbreviated, but we did discuss critical audit matters. Your feedback was very helpful. I think we may have time today if anybody has any further comments regarding that toward the end of this session.

But our focus, to start off with, is on the new elements of the report and the other information standard that is included in the PCAOB's proposals.

Since we are back on schedule and we have time, we thought that it would be helpful before we just open up the floor for discussion to provide an overview of the standards. And then we will get into the discussion. And then, of course, I expect we will have time at the end if there is anything else that wasn't covered that is of interest, certainly we would like to hear your views on that as well.
So, with that, I will turn it over to Jessica.

MS. WATTS: Thank you. As I mentioned yesterday, the proposed standard, in addition to critical audit matters, includes new elements. Specifically, independence and auditor tenure.

Related to independence, the proposed standard would require the auditor to include a statement in the auditor's report that the auditor is a public accounting firm registered with the PCAOB and is required to be independent with respect to the company, in accordance with the United States federal securities laws and the applicable rules and regulations of the SEC and the PCAOB. Under PCAOB and SEC rules, the auditor is required to be independent of the company.

This statement in the auditor's report is intended to enhance investors' understanding about the auditors' obligations to be independent and to serve as a reminder to auditors of these obligations.

Related to tenure, the proposed auditor reporting standard would require the auditor to include in the auditor's report a statement containing the year that the auditor began serving as the company's auditor.
Currently, this information is not required to be communicated by the auditor, management, or the audit committee to investors or other financial statement users.

Auditor tenure has been the subject of discussion for decades and investors and others have indicated strong interest in this information. In light of the public interest, we've proposed auditor tenure as a data point in the auditor's report. The intent of the proposed requirement is to disclose the duration of the auditor's relationship with the company.

And then the next thing we will talk about is the other information standard. So, during the Board's outreach process, some commenters had indicated that they would support changes to the auditor's report that describe the auditor's responsibilities related to other information and the auditor's conclusions related to the other information.

And in order to provide a basis to better explain to investors the auditor's responsibilities related to that other information, and the auditor's conclusions, we determined that changes to the existing other information standard were appropriate to provide a specific basis for
this description in the auditor's report.

As a result of this link between the proposed auditor reporting standard and the proposed other information standard, the financial statement user would obtain useful information, such as the nature and scope of the auditor's responsibilities with respect to other information, clarification of what other information was evaluated by the auditor, and a description of the results of the auditor's evaluation of the other information.

The other information standard specifically applies to a company's annual reports filed with the SEC under the Exchange Act that contain the company's audited financial statements and the related auditor's report.

The proposed other information standard would require the auditor to evaluate whether the other information contains a material inconsistency, a material misstatement of fact, or both, based on relevant audit evidence obtained and conclusions reached during the audit.

In addition to reading this other information, the auditor's evaluation of the proposed other information standard would include performing procedures intended to help the auditor identify whether the other information
contains a material misstatement of fact or a material inconsistency. The proposed other information standard provides specific responses when the auditor identifies a material inconsistency, or a material misstatement of fact, or both, such as communication with management and further procedures as necessary.

So, now I will turn it back to Jennifer to start our discussion.

MS. RAND: Okay, thank you. So, to start off, we would like to talk about the new elements in the report, specifically the element regarding independence, a statement from the auditor about independence, and also on auditor tenure.

I see Loretta. Loretta, go ahead.

MS. CANGIALOSI: Good morning. On the independence, I don't have an issue. On the auditor tenure, I guess my question is, as I read this, it seems to be far reaching backwards, particularly with predecessor firms, because, as we know, audit firms have merged over the years. And one of the things I really would like to hear from investors is how relevant all of that is.

Because if you have been audited by the same firm
for 15 years, 20 years, 30 years, I mean, when does that really strike them as a hot button? Because going all the way back, you have a different management, different partner, different firm. Having previously been with Main Hurdman and then KMG, I can tell you that when they merged with KPMG it was a different auditing set of processes. So, I'm not sure how relevant the predecessor firm is. And also, you know, the fact is that if we are looking for independence, when you have different management teams and different auditors and audit firms, again, I don't think you have that independence issue as striking. But I am interested to know if there is a cutoff by which investors believe that it would be satisfactory to say they've been our auditors for over 25 years, rather than going all the way back.

MS. RAND: Okay, thank you. I think it would be helpful to get some other views on this topic and we can go back and respond. But, Gaylen Hansen.

MR. HANSEN: Yes, if I could comment on both of these. Auditor independence. So, certainly the audit report is titled, "Report of Independent Registered Public Accounting Firm." So, there is sort of an implied
conclusion that the firm is independent.

It's interesting the way the paragraph is written. It says that the auditors are required to be independent. It doesn't actually say they are independent. And I understand the argument that there is violations, a lot of times very minor, that are resolved with the SEC, or with actions as taken, so that the firm can be independent during the course of the audit. But, for me, it's sort of a disconnect.

If the auditor can't say affirmatively that they are independent, I think there's an expectations gap problem with that in the report itself. So, I would like to see a stronger statement here. And I'm not sure exactly -- I don't know that I have the solution for that, but we have to make it clear that the auditor is independent in the way that it's communicated to users.

And then on tenure, I don't particularly have any problem at all with the disclosure of that. It seems to me that -- and the issue has been raised with me by others. It may be important as to any implications as to tenure on independence, and the placement of that in the report could be important. If it's next to the discussion of
independence, maybe there is an implication that if there is some period of time that you have been the auditor that you are raising issues about independence. So I think we need to be careful about the placement and the manner in which it is disclosed. Thanks.

MS. RAND: Gaylen, did you have any thoughts about placement? It sounded like you thought an alternative might be preferable. I just didn't hear if you had made a suggestion or had any thoughts.

MR. HANSEN: The suggestion that has been made to me was that if it could be -- if the statement about tenure is not in the independence paragraph, it would be preferred. And maybe right near the end of the report, somewhere near the auditor's signature line.


MR. HIRTH: Thanks, Jennifer. To pile on on the tenure comment, I had polled a number of CFOs and audit committee members and I got some consistent comments around tenure. And let me just kind of read you the sense of one. "I don't like the proposal to disclose audit tenure. It would be or is out of context being placed directly in the auditor's report, and for long-serving auditors, implies
a taint on their independence, which I believe is unfair. We have independence rules. And either the auditor complies or not, irrespective of the tenure."

To add on to that, one option around placement would be to put it in the proxy, where there is discussion about the auditor and approval of the auditor. And you could put it there.

Now, Bob and I were talking about whether that is voluntary and suggested and companies just decide to do that or it's a requirement. So, that is a comment on tenure.

MS. RAND: Okay, thank you. Elizabeth Mooney.

MS. MOONEY: Thanks. I didn't get a chance to make some comments yesterday. So, I have a couple as well that might relate to yesterday's discussion, a couple comments. Just on the tenure, from my discussions with analysts, they are interested in knowing how long the auditor has been in place on an engagement with the company, but I can't say there's a consensus around how many years. But they are very interested in that time frame.

And I wouldn't make a blanket statement that it's a taint. I just think it is helping to educate the investors. But it is something that they like to know.
And we have gone back and tried to piece it together with annual reports we can get our hands on. The analysts have asked me to do that.

So, I would just say it is relevant and I don't see why -- you know, it's a fact. It is a discernable fact, and where it is, I mean, I don't see why it would be a problem in the auditor's report.

Just another general comment. We talked a little bit about IAASB's proposal yesterday, and I just would encourage PCAOB not to wait. Convergence has been a slow process, and just be a leader and do what the Board thinks is the best thing. And, hopefully, convergence will happen naturally.

In terms of what information would be especially useful, you know, I think one important piece is the risk assessment and how it changed during this year, or this audit, from the prior period or periods. And, you know, the biggest risks and how the risk auditors responded to them, how much time is spent on them, how they got comfortable with them, any significant adjustments to the work they did. That is the kind of thing that would be really useful. And, again, it is about the audit.
And in terms of reporting the critical matters, I would just encourage you to make sure that the standards are strong enough. It should be really based on what's required, what is significant, according to the audit standards. I think this came up in your IAG meeting, but I think that's really important so that you can have some consistency and that it will be actually an enforceable standard.

And on the other information, you know, outside of the financial statements, I think if auditors know that investors are getting certain bad information, it's their responsibility to say something. So I think to fix it or do something, that makes a ton of sense.

Thanks.

MR. BAUMANN: So, before we take -- there is a lot of other cards up -- I thought we would pause just for a second because a lot of comments were made. Maybe I will add some color and see if it helps or not.

So, the thought on the tenure, because a lot of points have been made that it's not relevant and firms have merged and different partners change every so many years, and therefore to some it's not meaningful or some said it
When we had hearings around the concept release on auditor independence, objectivity, and professional skepticism, including rotation, there were a lot of people who testified at those hearings and talked about concerns about long tenure. But at the same time, there were some people that testified and said they're concerned about rotation because they think the riskiest audits are in year one. So there was a lot of points that came out of those hearings about pro and con rotation with risks in both directions.

So the thought on putting in tenure was, well, for those investors who think it's very risky in year one of a new audit, of an audit, for an auditor that really isn't up to speed, potentially, on all the issues in the company, that's a valuable data point for that investor that has that concern.

And there are those others that have that concern that 120-year relationships, even though partners do change and firms merge, firms tend to value in a certain way their 100-year relationship clients or long-term clients. And there is probably some pressure on the audit partner,
besides just doing a good audit, to not be the partner that
loses that client that has been a client of the firm and
a crown jewel of the firm for 100 years.

So, there is enough pressure doing the audit itself.
But to be the partner who is going to make tough calls that
might cause losing the client puts extra pressure on him.
So maybe investors want to know about those relationships,
because they feel those partners are under a unique kind
of pressure.

So, tenure really is thought to be a data point of
value, whether it's the first year of an audit or the
hundredth year of the relationship or somewhere in between.

But the comments you're making, I think, are some
of the comments we have heard across the board. Some people
think it is not valuable and other investors have said we
think it's a valuable data point.

So, I thought I would just add a little color.
We're not just pointing out the lengthier tenure. It's
whatever it is that could be potentially of value.

With respect to the comment on independence and the
fact that we are "required to," as opposed to "we are
independent," I think, Gaylen, you touched on the exact
issue, and that is some firms have violations of independence rules during the audit. And if they have a violation, that might affect -- they violated the rules that year. So, the statement is written in a certain context.

I think we will continue to explore that, because I think your reaction is a fair one and I think others have that. But I think it's something we have to work through.

So, I thought I would just add those points as we take the rest of the comments.

Jennifer, did you have any other additional reactions?

MS. RAND: No.

MR. BAUMANN: Okay, thanks.

MS. RAND: Okay, next on my list is Steve Buller.

MR. BULLER: Thank you. Just thought, a couple thoughts, again as a user. So, we rely upon the audit firm to tell us if they are independent. It's hard for a user to understand if an audit firm is or is not independent. And additional disclosure is not really meaningful information which is actionable for us, as an investor, merely stating that they are independent.

I guess while we have the SEC in the room, the thing
I would encourage, actually which is probably of more benefit to us, is to have a full review of the auditor independence rules. Because between the investment company complex rules, the 21010 over-under rules, the former partner pension rules, they are difficult for the audit firms. They are difficult for users also. We have two full-time people who spend all their time, 100 percent, monitoring auditor independence with contracts and relationships and former personnel.

But, also, it's apparent to us, at least, that there is going to be a higher degree of auditor rotation. Now, whether that is one percent or 20 percent, I don't know. But unless someone goes back and just looks at the issue of former partner pension plans and unfunded pensions, you know, as we have more and more former partners who serve on boards, including our board, if there are rotations we're going to see more required changes because of partner pension plans and taints as they bring in new audit firms. So, I just encourage the SEC to look at that as part of this longer term project.

With respect to audit tenure, we don't object to disclosure of the number of years in which the firm as served
as the auditor. Again, the question is what is actionable for us.

    So, for us, we think it probably makes more sense to have that disclosure in a proxy in the auditor opinion and here is why. If we think that there is a problem with the auditor independence or the number of years they've served, the way we take action is by voting in a proxy to not reappoint the auditor.

    It is hard for us to take action when we review financial statements to understand what it means and the impact upon financial statements if they have been an auditor for one year or 50 years. It's just not something that goes into our analysis of the integrity of those financial statements. It probably belongs in our decisionmaking of whether or not to retain the auditor.

    So, those are a few comments.

    MR. BAUMANN: Thanks for those comments, Steve. They're very helpful. I think actually a couple of them though are really for the SEC more than us.

    And somebody else also had mentioned earlier that they had thought, maybe it was Bob Hirth who mentioned that he thought if tenure is going to be disclosed, it should
be disclosed in the proxy, rather than in the audit report.
So, that is outside the scope of our authority, again, but
we take that point and appreciate that. So, the SEC has
heard your views.

MS. RAND: Okay, Professor Cox.

MR. COX: So, it was my pleasure, although it
interrupted a vacation, to testify, give some testimony at
the Roundtable on Auditor Rotation in San Francisco a couple
of years ago. And my actually eagerness to do that was
informed by the fact that before I even had the opportunity
to do that, I had started looking at the literature about
what the implications were on the question of independence
and tenure. And I was astounded. It was sort of like a
Goldilocks situation. And that testimony is all a matter
of record. People could look at the studies that have been
done, which I think I tried to correctly summarize.

But really it's a Goldilocks moment because it's
like the question about it's either too short or it's too
long and how the empiricists have been able to document the
problems that arose from this. And the studies all
indicate the following, that it's very hard to figure out
what is just right. Okay?
And we moved past the question of mandatory rotation of audit firms, at least at this moment in time. But it does make me think that what we would like to do is shine a light on this problem, because the problems are not only at too short a tenure, but the problems also exist, again, with some statistical significance, with too long a tenure.

And the whole function of what we are talking about starting yesterday afternoon and continuing this morning is where is an appropriate place to shine a light on this. And some things probably need to be centralized and located in one place. We all know that when you change an auditor, that's an 8-K filing that you have to make with the SEC. But there are some other things we may want to think as well, and that there is a central location of this very ever-growing set of financial statements where we would like to have some things just highlighted. And I think auditor tenure is one of those.

So, I think that just specifying what the length of the tenure is in the audit statement, in a very crisp statement, can at least shine a light on it and let investors do what they want with it. Some have staffs of two people who do nothing more than that. I'm going to suggest that
a lot of investors don't fall into that category. But by being able to highlight it, maybe they can dig into the question more likely and figure out what to make of the question about too short or too long a tenure.

MS. RAND: Thank you. Rick Murray?

MR. MURRAY: Thank you, Jennifer. I think there is a terminological problem that requires some further attention. The concept of being independent really is two separate thoughts. One is the condition of being independent, which is, generally speaking, capable of objective identification and explanation. The other is the way of doing things, which is a process, a state of mind, and a far more subjective and nuanced issue.

I don't think it's clear in the materials whether one or both of those uses of the word are clearly intended. It seems to me there are places where you would imply one thought attaching to the way independence is used and other places where it seems more to be the other.

So, I would encourage a review of the drafting process, so that whichever of those the Board intends to be the purpose of independence for this purpose is clearly specified.
Second, and a briefer comment, there is a catch-22 here in that, for 40 years, there has been a debate about whether it is possible, at least theoretically, to be independent when being compensated by the client. And there are, clearly, many voices who continue to believe that it's not and that it is a misrepresentation, if you will, for an audit firm to declare itself to be independent in the current context of the way compensation is arranged.

For those voices, some in academia, some in a variety of other communities, the use of litigation as a tool to challenge that alleged misrepresentation, and to use this new element of the audit report to accuse the firm of overtly misrepresenting their status as independent, if that is the way that the Board elects to use the word, is an unintended consequence that I think needs some attention. It can be clarified by defining a little more closely what the standards are that are being used for that purpose.

But when you ask the auditor to make a self-declaration of that, it ought to be clear whether the declaration is one status or of process and how that can be recognized by the regulator as an accurate statement,
in light of the compensation of auditors.

MR. BAUMANN: I would like to explore that a little bit, Rick, if we can. That's a very interesting comment. I think the first thought is, by including a statement in the audit report that we are required to be independent, according to the rules of the SEC and the PCAOB, our intent in drafting that and putting it in the report was we thought that that had a chance of increasing the auditors' thinking about their decisions that they had to be independent of mind and had that objectivity in the decisions they were making as they were coming to their conclusion on the financial statements. It might have that intangible benefit of increasing that independent state of mind that you talked about that's one of the couple of aspects of independence. I think that is the main reason for putting that there.

We would also like to put in the statement "we are independent," to Gaylen's point, but there are some other technical issues with that.

But I would like to explore what you meant by this has a liability and litigation issue and overtly misrepresenting the auditor's position. So maybe you
could share with me a little bit more your thoughts in that regard.

MR. MURRAY: First and most simply, Marty, if it is clearly the intent of the Board that the reference in the audit report is to the state of mind, the process, rather than the independence, that goes a long way. If that is clarified, that goes a long way to take both of my comments out of play.

MR. BAUMANN: Well, it didn't mean to say it ignores the fact that we had to comply with rules as well and that we are required to comply with rules. But, certainly, there are the two aspects. There is the rules and the state of mind.

MR. MURRAY: I may be wrong factually on this. But it is my impression that neither the SEC nor the PCAOB have ever overtly said we have examined the nature of the compensation of auditors in this system of financial reporting and we have concluded that that does not impair the auditor's ability to function independently.

If that were to be clarified and the declaration in the audit report were to fit into that model saying we have functioned independently, I think that reconciles the
problem. It's the overhang of a historical and not formally resolved question about the effect of compensation, coupled with asking the auditor to make a self-declaration that, if claimed to be materially misleading, which is certainly within the reach of trial lawyers these days, that creates the concern.

MR. BAUMANN: Thanks. I would be interested in others' reactions to that, but I understand the point you are saying, that potentially the client pays model creates a conflict that inherently affects independence and therefore making that declaration raises the point that you are concerned about. I don't know if anybody has a reaction to that, but if they do, I hope to hear from them as part of the discussion.

MS. RAND: Okay, thank you. Jeff Mahoney.

MR. MAHONEY: Thank you. I just wanted to agree with the staff statement that there is strong investor interest in the tenure information. That's reflected in our corporate governance policies in at least two ways. First, with respect to shareowners' oversight of the audit committee, our policies related to audit committees indicate that tenure should be a factor that the audit
committee looks at with respect to the retention issue.

MS. RAND: Jeff, I'm sorry. We were getting -- obviously, you are hearing that noise, but I was missing some of what you were saying. It was quite distracting. It seems like it has subsided. If you could just repeat that again. I apologize. I don't want to miss your point.

MR. MAHONEY: Sure. I wanted to express my agreement with the staff statement that there is a strong interest by investors in the tenure information. That's reflected in our corporate governance policies in two different areas. First, with respect to shareholders' oversight of the audit committee, in our policies related to the audit committee, we do say that the audit committee should look at auditor's tenure as one of many factors when considering auditor retention issues.

In addition, we ask for disclosure by the audit committee. When the auditor has been retained for ten consecutive years or more, that there be some additional disclosure by the committee about that decision to retain the same auditor beyond the tenure period.

It also has relevance with respect to our policies which many public companies have adopted with respect to
the annual shareowner vote on the ratification of the external auditor, where we believe that the tenure of the auditor should be one factor. Again, not necessarily the most important factor, but one factor that shareowners should look at when making that retention vote, which, as I indicated, is a very common at a large number of public companies.

With respect to where the information is disclosed, we do not have a policy saying that the tenure information should be disclosed in the auditor's report or in the proxy statement. I can see the argument that it be disclosed in the proxy but I'm not aware of anyone in our membership who would be upset if that information was disclosed in the auditor's report, which is the main vehicle of communication between the external auditor and shareowners, rather than in the proxy statement.

In addition, I think if you asked them if it's disclosed in the auditor's report, you may get this information in a shorter period of time -- you may get this information in a few years. If it's disclosed in the proxy, it may be a long time before you ever get that information. If you add that to the conversation, I think a number of
our members would agree or support the idea of having tenure disclosed in the auditor's report if they think they are more likely to get that information sooner rather than later.

Thank you.

MS. RAND: Thank you, Jeff. Bob Guido.

MR. GUIDO: Thank you. I just wanted to pick up on a couple of points, especially -- there goes the hammer. But what Steve Buller said about independence, and not to dwell on this issue too much, but go back to the premise that we on the committee spend a lot of time in this area, and we do challenge. And I would like to just remind everyone that tenure, from an audit committee's perspective, is one year at a time, which means the firms have to prove themselves, not only in performance on an annual basis but in the independence, objectivity, et cetera. Fact and state of mind.

Therefore, if something -- and I really believe that disclosing this in the auditor's report is out of context. Put it in the proxy where, if we want to, make it voluntary. I will bet you if you do best practices, there will be a lot of registrants that will follow suit. But it could be
couched within the audit committee's report, where we, in effect, challenge performance and reappointment.

However, if that doesn't fly, I have another suggestion. Ten years ago, we used to file with the PCAOB all of our registrant information. I don't know if that is still being done but I assume that it is. Why don't we just have the firms put in there how long they, in effect, have been a client? And that has access -- it used to be public information maybe it isn't anymore. But any investor that is interested could access that public information in a few seconds.

So anyway, just a thought.

MR. BAUMANN: Do you have a reaction to the comment that Jeff made that to the extent investors think that this is important, this is a proposal that we get this out to investors potentially in the near term. Whereas, if your argument is, maybe it belongs more in the proxy, there is no action taking place right now or no proposals on the plate to put that information in the proxy, other than voluntary. And there are some companies that are voluntarily disclosing that but there is no action underway, as far as I know, to put it required in the proxy.
MR. GUIDO: Well yes, I don't know of any action either. I do know that some registrants already put it in the proxy. And working with NACD and others, we could get this going, if that is so important to investors.

But again, I will go back to what I said before. For audit committees to opine on independence and performance, we do represent shareholders. And therefore, we have already concluded on that issue.

However, if we want to have it in the sunshine, put it in these reports and the firms file them annually, I believe. They still do, I hope.

MR. BAUMANN: They do. That is a form 2E you are referring to and that is available. Of course, an investor would have to do some searching to find not only the firm but then the issuer and so on and so forth. But it is an option, I am glad you pointed that possibility out.

MS. RAND: Okay, Jerry de St. Paer.

MR. DE ST. PAER: Thank you. I guess this is going to feel like piling on but I think my perception of it, while consistent with the views, for example, that Bob just expressed and others, it has a twist to it.

I chair one audit committee. I am on another audit
committee. In every one of the audit committee meetings, we take pains to confirm with the auditors that they understand that they report to us, the audit committee. They don't report to management. We make that very clear. We make it very clear that they have access.

But the other thing that is very clear is that the responsibility for taking -- I thought the comment by Professor Cox was very interesting -- too short, too long. The audit committee is where the buck stops in deciding whether it is too short or too long or what the other factors are. It is not the auditor.

I mean with all due respect, the auditor can have their views of it but who actually decides whether you are going to recommend the appointment of that auditor for another year, as Bob says, one year at a time? It falls to the audit committee.

So, I hear the point about the issue about timing, that if you put it into the auditor's report you are going to get something sooner. But it absolutely is out of context because it doesn't include the judgment of the people who are actually making the decision whether the independence is adequate for reappointment or not. That is
the audit committee.

So, I guess I would urge -- we have got Brian sitting here. We could all go beat up on Brian to try to get something moving at the SEC or to get the NACD or others.

I think that what I am focused on here is what is right and not what is expedient. I can understand why investors find this information meaningful. I completely get that. I completely also understand and sympathize with the view of the PCAOB to try to do something about that. I just think that we have got the ball in the wrong place.

I think to have an auditor to say they think they are independent is fine but I think it misses the fact.

The second thing that I wanted to express, and it has to do with this auditor independence when I read the proposal, and it goes to a little bit the concern I had yesterday. You can't get away from your roots. Having been CFO of an insurance company that does auditor liability insurance, the fact is here what will happen -- and then if you sit on the audit committee and lawyers come in and they say okay, we have got these new rules -- what will happen I am afraid, and this is the thing I would urge that -- and I don't know how you deal with this because I
I understand what you are trying to get on the CAM. I understand what you are trying to get on auditor independence but the pressure toward boilerplate is going to be so strong.

I mean can you imagine that this new thing comes out. We have got the new CAM. We have got this, and then there ends up being a problem. It is like a roadmap to litigation.

So what is going to happen, I predict, is that it will go overboard. There actually is no incentive for anybody to do anything other than to throw the kitchen sink in and call it material.

So, unfortunately, you should never make a suggestion. On the first instance, my suggestion is put it in the proxy. On this one, unfortunately, I don't have any helpful guidance, except that I could just see this thing blowing out the auditor's report significantly into a big document, which will be almost unfathomable for the average investor to be able to understand.

MR. BAUMANN: That is a risk certainly we are concerned about. We are concerned about boilerplate. So the things that you brought up are good points that could
risk the value that we are trying to bring. So, we will carefully think about those issues.

Brian's card promptly went up when you talked about the SEC. So, we will give the floor to Brian Croteau.

MR. CROTEAU: Thanks, Marty, and good morning.

I guess first I just wanted to say I don't feel beat up upon at all. I think it is really important that we all hear these comments. And again, my disclaimer from yesterday still applies as well.

But certainly geography can be extremely important and we do appreciate the comments in that regard and particularly when we are talking about matters that may have to do with whether you are evaluating the engagement of the auditor, versus the report and the completion of the audit. We certainly can appreciate, or I can appreciate, the differences between the two. And so I don't think people should feel restrained in offering whatever feedback they think is appropriate about either the nature of the disclosure or the appropriateness of the location. And certainly me and my staff are here and others are listening to take good notes on that. So, I appreciate the feedback.

MS. RAND: Okay, thank you. Oh, sorry. A number
of cards are up and then I would like to try to get to other
information.

But next on my list is Walt Conn.

MR. CONN: This may also feel like piling on at this point, but I will take Brian's invitation.

In the interest of transparency, I fully support the disclosure of auditor tenure in a place that is easy for investors to find. I would argue, though, that including it in the auditor's report, just to echo some of the other comments that have been made, implies a correlation between tenure, a sweet spot for tenure from shortly after first year, second year, whatever that may be, to whatever a long tenure is, a sweet spot between that and audit quality that I don't think is known today. And therefore, I agree with the comments that have been made that it seems out of context to be in the auditor's report and it seems like to me the best place would be in the proxy or in the Form 2.

Thanks.


MR. PLATT: Thank you. The point has been made by several people that the consideration of tenure really is a question of reappointment of the auditor and the audit
committee's responsibility and the audit committee's focus. And many people have observed that maybe it is better placed in a proxy, which discusses the audit committee's decision to reappoint the auditor. I would actually agree with that.

And then others have said then that well, but because the SEC doesn't have a project currently, therefore, it will take longer to get through proxy than possibly what the PCAOB can do through mandating through an auditor's report. It kind of reminds me if the only tool we have is a hammer, we are going to think that everything is a nail.

And I wonder, though, whether or not there might be a way to accomplish it through saying that if it has not already been disclosed in a proxy, then the auditor will include tenure in the report. But if the company and the audit committee has included auditor tenure in the proxy, then the auditor's report would be silent to that fact.

So, it might be a way for the PCAOB to take action, which sort of goes along the way of encouraging proxy disclosure and many companies then will probably jump on that, and therefore, one place or the other you would end
up finding the disclosure of tenure information. So just
1 a thought, in terms of saying, you know, can you use the
2 hammer of the PCAOB to get disclosure either in proxies or
3 in the report itself.
4
5 MS. RAND: So Bill, just to make sure I am thinking
6 about it the say way as you are suggesting it, so you are
7 suggesting -- because generally the proxy is filed after
8 but you are talking the proxy that was filed before for the
9 appointment of that year.
10
11 MR. PLATT: Yes, the proxy that was filed before.
12 It would be a little different than now the incorporation
13 by reference of compensation information, which is going
14 to be in the next proxy, because you wouldn't necessarily
15 know what was going to be in the next proxy.
16
17 But if it was in connection with the appointment for
18 that year had been disclosed, then it wouldn't need to be
19 repeated in the auditor's report.
20
21 MS. RAND: Okay, thank you. Dan Montgomery.
22
23 MR. MONTGOMERY: Thank you, Jennifer. And just a
24 quick comment on independence to compare and contrast a bit
25 with the IAASB proposal because I know that many in the room
26 will be reviewing and commenting on both.
Like the PCAOB, the global stakeholders of the IAASB felt that there would be value in having a statement about independence in the auditor's report. However, the IAASB stakeholders, in particular global securities regulators, felt that there should be, along the point that Gaylen made earlier, an affirmative statement of independence. And so, the IAASB's proposal is to specifically indicate that we are independent of the company within the meaning of the relevant ethical requirements or applicable law or regulation and have fulfilled our other responsibilities under those ethical requirements. Also, it would be required to specifically identify the relevant ethical requirements.

And the IAASB, in formulating that language, also considered the notion of breaches. And maybe this is something that works in the international arena because there is a recent revision to the International Ethics Code that suggests that if there are any breaches of independence requirements, the auditor is required to communicate those with those charged with governance. And if the auditor believes that appropriate action can be taken and those charged with governance agree, then the auditor is able to
affirm independence and issue an independent auditor's report. So the affirmative statement about independence, at least in the IAASB view, would work in that regard.

MS. RAND: Thank you, Dan. Roman Weil.

MR. WEIL: I have not necessarily been paying attention but I am confused about the auditor tenure and the disclosure that we have in mind here.

In the audit committees where I serve, we have got an audit partner. We have got an audit partner in waiting, the guy that is going to be the next audit partner. We have got the confirming partner. We have got the partner who resolves conflicts if something comes up. He is sort of in the background. And we have got the seniors and managers.

And in our audit committee reports, we have got a table where every one of these people, who they are, how long they have been serving, and when the audit company's, audit firm's rules will require that person to go off. Sometimes the audit company's rules are more stringent than the SEC rules or the regulator's rules. But they will tell us how long he has been there, when he has to go, and what the plan is for taking over.

Now, I can't tell from any of this discussion, when
we are talking about auditor tenure, are we talking about one person or are we talking about the whole team? If it is the whole team, I think that is fine and we get it already. I just don't see what the big deal is.

MS. RAND: Tenure would be the firm relationship. So, there would be natural rotation of the partner, for example. But to Marty's example he used earlier, the firm may have been auditing a company for 100 years. There is rotation of the individual partners every five years, but the question is, some perceive that the 100-year relationship, even though there is the individual rotation, may have added pressure for those firms.

MR. WEIL: So that word "auditor" means the firm, not the person.

MS. RAND: Auditor means the firm, yes. Right, firm.

MR. WEIL: The firm, okay.

MS. RAND: Okay, I don't see any further cards up, so I am going to move on to other information. And thank you for your comments on both of those points. I think it was very valuable. Some good questions and suggestions came out of that.
For other information included in the PCAOB's proposal, as Jessica described, there was a proposed standard regarding the auditor's responsibilities for other information regarding the annual report that is filed with the SEC. So, that would be the 1934 Act filings, generally, the 10-K.

So, interested in your views on the usefulness, including a statement in the auditor's report about the auditor's responsibilities for other information. The proposed language in the report would state that the auditor has read and evaluated the other information.

The auditor's responsibilities include looking for both material inconsistencies with the audited financial statements, so looking at amounts and disclosures in the audited financial statements. If revenue is stated at $100 million, is it $1 billion in the 10-K? That would be a material inconsistency. So, they are looking for consistency with the financial statements.

And the auditor also would have a responsibility to look for material misstatement of fact. They have both these responsibilities today but a material misstatement of fact could be the auditor knows through their audit that
the company is a manufacturer of widgets. They are not the
leading manufacturers. Say they are number three. But in
the 10-K they have disclosed that they are the leading
manufacturer of widgets. The auditor may believe that
would be market moving information if the public believed
that they were the leading manufacturer. But based on the
auditor's audit, obtaining understanding of the company,
they know that is incorrect.

So under our proposed standard, the auditor would
have a responsibility to discuss that with the audit
committee to have that be removed, clarified.

And the proposed standard also includes procedures
to evaluate the other information. Today, the auditor's
procedures are read and consider. That's it. It is
whatever the auditor does in connection with consideration.

We have read and evaluate. And evaluation means
four different types of procedures, such as comparing the
amounts with the financial statements for consistency,
looking at the disclosures, taking into consideration the
other information the auditor knows, is there any material
misstatements of fact, and looking at calculations that are
presented in the other information.
So, I will just open that up generally for views on other information and you can feel free to touch on any or all of those points.

Ian Dingwall.

MR. DINGWALL: Thank you. As I read this report on other information, it presumes the other information is in fact presented. In other words, it is a report on that which is presented. It is not necessarily a report on things that might be required but are not presented. In other words, we do require in 11-K filings or in plan filings, that a lot of other information be presented.

The problem usually is that it is not presented. It is not there. So, I would think that this report on other information could be more valuable if it talked about the completeness of the information, or it made some reference to the fact that none of the required information has been omitted, something along those lines.

Just to say what is presented is fairly stated in relation to the financial statements taken as a whole is fine but it would be, I would think, more valuable if it suggested that the information that is required to be there is in fact there.
So opining that nothing has been omitted, I think, would add to the value of this report.

MR. BAUMANN: So let me just comment on that, Ian, just to clarify a couple of things.

So, the other information, of course, we are talking about is in connection with the '34 Act filing. And what has to be there is in accordance with the SEC rules in connection with that particular '34 Act filing for either a corporation, or a mutual fund, or whatever it might be in that '34 Act filing.

We did ask in the concept release on auditor reporting, should auditors have some further responsibility to examine the other information? And generally there was not support for that. To the extent that there was support, I think there was support for the auditors' continuing responsibility to read other information and consider whether it has any material inconsistencies with the audited financial statements or material misstatement of fact.

So, there is not a requirement in existing standards, and we are not proposing one, for the auditor to extend his or her responsibilities to ensure that the
company has fully complied with all of the various aspects of the SEC rules as to what has to be in MD&A, what has to be in risk factors, what has to be in the various aspects of the '34 Act filing. That would be a separate engagement. Legal interpretations would be involved in terms of what would have to be included in that information.

And so that is not the extent of our proposal at this point. We have heard your view that you think that would be valuable to the auditor to do that. We haven't proposed that and we really hadn't heard a lot of support for that, but I will be interested to see if others do that.

The comment that something is fairly presented in all material respects went to something I discussed yesterday on supplemental information that is related to the financial statements that is required by SEC rules to be part of the financials. But it is supplemental.

With respect to the other information that we are talking about here like MD&A and risk factors, there is no opinion being expressed on that information. It is a matter of we have read and evaluated it and we are not aware of any material inconsistencies or material misstatements of fact. Now, that is some type of assurance but it is not
an expression of an opinion.

I don't know. Hopefully that clarified it, if anybody had any confusion as to what the requirements were.

MS. RAND: Thank you, Marty. Denny Beresford.

MR. BERESFORD: I think this part of the proposal could be one of the more useful additions to the auditor's report. And in the concepts release I, and I think a lot of other people, supported it with the sort of implicit understanding that at the time the idea was simply to have the auditor report explicitly on what was already being done.

But the proposal, and looking at one of the earlier slides, indicates that this would enhance the auditor's responsibility with respect to other information and, these are the key words, "by adding procedures for the auditor to perform in evaluating the other information based on relevant audit evidence obtained and conclusions reached during the audit." Adding procedures, I guess, would be the key words.

And in looking at the releases that came out shortly after the proposal by at least two of the major firms, and I suspect the others agree at this point, they characterize
this as substantial additional work that would have to be performed. At this point, it isn't clear what that exactly means but it sounds like a very major undertaking that the firms see. Reading the document, it is not clear exactly what the PCAOB has in mind. And it is not clear, of course, to me what the firms have in mind that they would have to do.

One obvious concern is that without a lot more specificity, this could turn into another PCAOB auditing standard number two versus five kind of situation where something is put out along the lines of what you have right now. The firms think again lots and lots, and lots, and lots of additional work. And then we find out that is not really what was necessary. But in the meantime, we have added, pick a percent, 10 percent, 20 percent or whatever to our audit fees and so forth for minimal additional benefit, if any, to the users.

Again, I think going back to my beginning point, if we were simply asking the auditors to report on what they were already doing, in other words, that they had, as part of existing standards, reviewed the other information in connection with the procedures that were already part of
the audit and found it not to be inconsistent, and simply stated that with appropriate caveats in the report and so forth and not putting subheadings in and other information that would lead the users to believe that this was subject to a lot of additional auditing and so forth, I think that could be a major step forward.

I guess my major concern again is would it really be worth it to add a lot of additional procedures to create something that would not be fully audited in any event.

I guess my major suggestion here would be that I think that this is something that would really -- I would urge you to be very careful. And I'm not sure exactly how you do it but I think you need to do some field testing. And I don't know how you can field test something in advance but I urge Marty that you work with the accounting firms and get an understanding of what do they mean, what do they have in mind in terms of all these additional procedures that would have to be performed and compare that to what you believe are the added procedures that would be necessary to meet the requirements of the proposed standard and try to have a meeting of the minds in advance, as opposed to putting out a standard that would then be, in effect, not
operational or be subject to a lot of ambiguity, again, like the unfortunate situation we had before.

Given the existing situation, given the uncertainty about what is going to be performed, I don't believe that it is supportable in its present form but if it can be, you might say, rolled back to just reporting on I think it is AU 550 approach, then I think that would be a very good step forward.

MS. RAND: I just want to react to a couple of points you made. Kind of what you are suggesting at the end, your recommendation that we just stay with the standard that we have. Our challenge in using the standard we have today and having the auditor's report on that is the auditor's responsibility is read and consider.

And there are no procedures about what does consider mean. So, one auditor may do all these procedures and more. And we heard a lot in our outreach because we did ask, that was one of the alternatives in the release, if the auditor should perform additional assurance. We received a lot of feedback that auditors do a lot today in connection with consideration. But what is not clear to users is what is meant by consideration. One auditor could do a lot.
Another may read and not do much with it. So, we are looking for consistency in how auditors are reviewing that information. We do consider it important information, that there is no material inconsistencies, material misstatements of fact because the auditor's report is included in it. So, they are associated with that document.

The evaluation, the procedures in there, you compared a significant amount of work. Interested in reaction from the firms, our experience in developing the standard, we thought it was reasonable procedures. Again, it was consistent with outreach that we had conducted that auditors are generally performing a lot of work, a lot of these types of procedures, checking consistency of amounts. Checking to make sure that disclosures, what is in the financial statements, is not inconsistent with how it is being presented.

So, interested in other views on that, but just wanted to react to some of your points.

And Marty, do you want to add on?

MR. BAUMANN: Well, no, I don't want to add on but I want to concur with Denny that we don't want to create
an AS 2-type environment. So, that is the reason why we put out a proposal and have SAG discussions around it. And hopefully, we will get comment letters that will -- if there are concerns around the nature of this, that it is not understandable or it is ambiguous or there is too many procedures, we will get those comments and certainly react to that.

There is at least some of us who have audited large companies at the PCAOB who, when we looked at this, said this is basically what we thought was pretty much existing practice in major corporations, at least, that basically the auditors felt this was part of what they did to read and consider. And certainly the audit committees and a lot of companies said we want you to read this information and make sure it is consistent with the financials. And if there is anything materially inconsistent, material misstatements of fact, certainly bring those to our attention.

So, I think our view is that a lot of this and these four procedures, so there aren't an extensive amount, there is four procedures, we felt was pretty much maybe a best practice that was already happening today in a lot of
corporations, although we thought that there was probably varying practice among the 10,000 audits in the country.

But your points are all well-made and we look for comment if it is creating confusion, ambiguity or more work than is necessary. So I am sure we will hear that from firms or others.

Thanks, Denny.

MS. RAND: Brian Croteau.

MR. CROTEAU: Thanks very much. And it relates to these points, I think.

And Denny mentioned these words, and I hate to get overly technical but I just want to be sure that we are all thinking of an aspect of this that I think is embedded in the comments that were just made.

But paragraph 4 contains the words that Denny was reading from a performance perspective that get at the auditor should read the other information. And "based on relevant audit evidence obtained and conclusions reached during the audit" perform certain procedures. Paragraph 13(c), which has the report, contains those same words.

And it occurs to me that users of the report may not necessarily know what all of the evidence was that the
auditor obtained. And so there is a limiting principle here relative to the auditor's work that has to do with what evidence the auditor gained in conducting their audit work. They are not expected, per the standard, although they may for other reasons but not for the standard, to go further and obtain more evidence in conducting this aspect of the work.

So, I think there is a limiting principle built in. Whether that is the appropriate limiting principle might be a question for people to comment on. And then how users will interpret the report, given that they won't know necessarily as a user what evidence the auditor obtained, I think is an interesting question that I would certainly be interested in feedback on either today or through the comment process.

But I thought I would just highlight that because I think that is an important element of what is being described here, relative to the limitations and what stops this from being a full audit, another element of what stops this from being a full audit, or something that is more like AS-2 if people think of it that way.

MR. BAUMANN: That is a good point, Brian. And we
intentionally, of course, put that limiting factor in, that
the auditor who performs these procedures read and evaluate
in the context of information based on relevant audit
evidence obtained during the audit. And the point is that
the auditor is not now intended to, supposed to -- not
required by the standard to perform additional procedures
to learn something about whether or not some product in R&D
is going to be launched next year or not, if that is the
statement being made in the other information, if that
wasn't part of what the auditor obtained as part of their
evidence.

And again, the procedures then are tied to, the four
procedures are tied to what the auditor learned as part of
the audit and then comparing that to what is in the other
information.

But I fully accept your point, Denny, that we want
to make sure that it is clearly understood.

And Brian's point goes to another issue, though,
that there could be an expectation gap with this statement
in here that we have read this other information and
evaluated it, et cetera, that someone might think they did
perform other procedures, even though it says in the report
we did not audit this other information, did not express
an opinion on it, and it was based upon what we learned
during our audit but it has that expectation gap risk,
potentially. So we wanted to get comments on all of that.


MR. BREEDEN: Thank you. I think the objectives
here are understandable and worthwhile. And certainly,
the notion, as a member of an audit committee, that the
auditor, in considering their work, has developed a
conclusion that there is a material misstatement of fact,
it doesn't seem radical that they should communicate that.

But the way this is drafted, material inconsistency
and material misstatement of fact, to me that sounds awfully
much like a violation of Rule 10b-5. That is fraud.

And so, asking the auditor to report on a
formulation that sounds like a legal conclusion of fraud
and if it is material and it is a misstatement of fact, it
is unlikely to be accidental. There is almost certainly
going to be an element of scienter in there.

Anyway, to me, I think you need to work carefully
to make sure we are not creating something that becomes a
rival legal review for the issues of fraud. And I am
worried that this would trigger something. It could either
be meaningless because the standard is such that if you are
not -- if you haven't reached a conclusion, if all the
element of a material misstatement are there, you wouldn't
report it. And yet, the obligation to make that statement,
if it is formulated in a way that is essentially a judgment
of fraud -- if you want to say that auditors should report
on any signs of potential fraud they have seen, that is one
thing. But this is a legal conclusion that you may want to
work on the formulation.

MS. RAND: Well, you raise a very good point. In
the standard, we do point the auditor to our fraud standard
when they identify material inconsistencies, material
misstatements of fact. I think we recognize there could be
a difference between the audited financial statements and
the 10-K could be just an error. But we do point the auditor
to consider the nature, you know, discuss it with
management, go back to the fraud standards to consider if
it is something more than that.

The current standard, under our current framework,
the auditor reporting standard would allow the auditor to
issue an unqualified report, even if there is a material
misstatement of fact. They could include a paragraph and say we believe the audited financial statements are okay but we have identified this material misstatement of fact.

We are asking questions about the auditor's responsibility when something is identified and not corrected in their continued association. Kind of along, I think those same lines.

Did you -- you look like you were going to react to that.

MR. BREEDEN: Just the further observation that auditors are not experts in general matters of fact. And so when you go beyond the financial statements and into the realm of any misstatement of fact without qualification, that really can -- and without very carefully delineating, as Denny and others have said, what you have in mind, I think it would not be helpful to investors if you moved down the road toward competing 10-Ks. And the whole world of facts about a company's business that may be included in its reports get far afield from the financial information that the auditors are expert in reviewing.

So, that also is a slight concern of where this evolves to and making sure it is quite clear at the outset
because that is a path that might lead other directions.

MR. BAUMANN: Richard, thank you. Those are all good points and we really have to consider those, especially the auditors are not in a position to reach a conclusion, necessarily about violations of 10b-5.

I just will point out, however, that under existing standard AU 500, which is the read and consider other information, so there is an existing standard today which requires the auditor to read and consider the other information to see if there is a material inconsistency with the audited financial statements. And it does go on to say if while reading that other information the auditor becomes aware of a material misstatement of fact, the auditor should discuss that with the audit committee and consider other actions.

So, there is existing auditing literature already that has this. So, we have built on that. So but nevertheless, even though we are building on that, we will take into account the concerns and considerations that you have expressed.

MR. BREEDEN: You might be better off having something where if the auditor is aware of an apparent
inconsistency, they should discuss that, as opposed to keying it off a legal conclusion. And if the auditor is worried that what they have read is inconsistent with what they have seen, that is worthy of a discussion with the audit committee, and they shouldn't sit back and be having their own lawyers trying to evaluate has this crossed the line into an actual material misstatement of fact.

MR. BAUMANN: Thanks.

MS. RAND: Okay, Jerry de St. Paer.

MR. DE ST. PAER: Thank you. I seem to be in the piling-on mode today. But I hope from a little different perspective than the perspective that has been expressed, even though it supports that.

From the perspective of a CFO of a New York Stock Exchange company, with auditors who -- I couldn't tell you -- clearly, from their procedures, they were required to take a look at the other information, but we would never have issued it without them taking a look at it. So, I am not really sure what the chicken and the egg was there.

But I watched the way in which that procedure was done, and it goes to what Dennis said. There is a great deal of difference between making an affirmative statement of
this kind and simply following the procedures.

Again, one of those companies that I was the CFO of happened to be one who wrote a lot of auditor liability insurance. And I can tell you that will cause the kind of reaction that Dennis was concerned about, where to be able to make that kind of a positive assessment, to go to the 10b-5 or the SAB-99 issue, you are asking the auditor to take an additional step. So, I would just also argue the caution.

But I want to also make a second point that I think is really important, is that we heard in the presentation yesterday about the volatility of earnings based on release of earnings. From the experience, at least, in the companies I have been CFO of -- and when I was CFO, I was pretty interested in what the stock price did relative to the release of earnings -- that volatility is almost all related to the press release.

What happens when the K or the Q comes out is very little additional movement. And so the whole issue -- we also, by the way, had the auditors review the press release to make sure that there was no material inconsistency or misstatement of fact, just to make sure that we were okay.
But there is a lot of non-GAAP measures. The things that drive the market -- which is one of the things I thought was missing in yesterday's presentation -- the things that drive the market, with all due respect to the SEC and the design of all of the reports, isn't actually materially driven. It is at least equally driven by the non-GAAP information, in most cases, as it is by the GAAP information.

So, I just want to say while the concern about the risk you are creating by forcing this affirmative representation, to what Mr. Breeden said, is a big issue, and I am not sure it has got the elephant in the room. Because the thing that really is creating the biggest movement of share prices for the investors that are concerned about this information, actually it doesn't come out of the MD&A. What I found astounding in meetings with investors is that the questions almost always come -- they actually come before we ever issued the K or the Q. They came from the press release.

So, I would just like to caution to keep our eye on the ball here, that we are acting as if this other information is really the stuff that is driving investors.
And I guess maybe everybody here, all the investors, are going to say, oh, well, we look at all that stuff. I can say from my side, in talking with all my investors, that is not where the questions came from.

So, just in terms of priority, this will, I'm sure, involve additional scope and expense and I am not sure about the cost and the return.

MR. BAUMANN: Those comments we have heard from others. And I look to the left of the room over here to Mike. We have often heard about what really drives the stock price and what investors are really concerned about is probably in much earlier releases than the 10-K. So, we have heard, certainly, that comment before.

To some extent we are limited, in terms of the auditor's responsibility, that they have to audit financial statements and report on financial statements and what's associated with the financial statements, you know, their responsibilities can go to that, too.

At least right now, under our authority, I don't believe, speaking for myself only, that we could require an auditor to perform procedures on that press release. But we've heard that from Mike and from others that that
would be very valuable if auditors were required to do that. But at least speaking for myself, and only for myself, I don't think we could require auditors to do that under existing authority that we have.

But one thing I will add, many, maybe not all, but many of the -- much of the information that gets in that press release that drives the market at that time, and the non-GAAP measures, are also in that 10-K and are discussed in that 10-K. It's usually the same type of information around a non-GAAP measure or the performance that was previously discussed in a release is in the business section of the 10-K.

Management, knowing that the auditor is going to read and evaluate that 10-K, which includes probably those same non-GAAP which the auditor would have to, under these standards, see how they are reconciled to the financial statements to be not misleading and create a material inconsistency with the financial statements, I think has a deterring effect on management's behavior when they come out with that release, knowing that the auditor will be performing procedures on that information later on.

So, I fully acknowledge what drives it. But
knowing that that same information is likely to be in the 10-K, to be read and evaluated at a later date, I think has a deterring effect in addition.

So, I'm interested in your comments on that. I wish we could have the auditors do more up-front. And I know you want to comment even further. You're anxious to say something here.

MR. DE ST. PAER: I am. Because of the legal environment, at least in our case, we didn't release the press release until we had virtually a complete draft of the 10-K and the MD&A done because you could not possibly have a situation occur -- well, at least I don't think a responsible person could put out a press release where a few weeks' later you are going to put out a 10-K. You virtually have to be almost at the point where they auditors are pens down by the time you issue the press release, or you're taking huge liability.

And, actually, I was surprised Brian's card didn't go up because the truth is what happens if you don't put a reconciliation of the non-GAAP measures in the back of that press release or the supplement information that you put out which reconciles to the audited information, the
next call comes from the SEC. I mean, I have had the
opportunity to have that conversation with them.

And rightly. That is not a criticism. That is as
it should be. But there is a reconciliation and the audit's
not done. So, people don't put out press releases hoping
that they get within the range of the 10-K. Most companies
have this stuff all come together at the same time.

MR. BAUMANN: Thanks for that additional color and
valuable input. Walt Conn is next.

MR. CONN: Yeah, in my firm, we are still developing
our views on parts of the standard and particularly our
comfort with the words in the report.

But let me just circle back to Denny's question on
the procedures that are in here. I think, in general, in
my experience, these procedures are consistent with what
we do today. However, there are a couple of words or
phrases that give us pause and we're formulating our
questions or recommendations on those. But we want to be
sure there is clarity about whether the scope of our work
should expand beyond what it is today and whether our
responsibility should expand.

One of the changes that gives us pause is the change
from "consider" to "evaluate," because if evaluate means "do these procedures that are listed," period, then maybe that is okay. If evaluate means "do these procedures and whatever else you need to do to conclude that you have performed an evaluation," then that probably lacks some specificity that is needed.

The other change that gives us pause is that the reference to consistency with the financial statements, in the proposal now adds consistency with the relevant audit evidence. And that seems to be a subtle expansion beyond where we are today.

MS. RAND: Walt, to respond to that, you asked about what does evaluate mean. The way it's phrased in the standard, we have evaluation based on the procedures in paragraph four.

So I don't know -- and continuing your thinking on that, if you are just concerned about how that may be perceived in the report, but at least the way it is proposed in the standard, it's based on those four procedures in paragraph four.

MR. CONN: Yeah, and we realize that, and are just struggling with that choice of words, whether it will be
clear to all stakeholders that evaluate means "just perform these procedures." Because we think of evaluate as not being limited to specific procedures but going beyond that.

MR. BAUMANN: Good points and we'll think of that as we consider where to go with this. But it was interesting to hear your comment that you think largely these are the nature of the things you do today, but with a careful looking at each of the words to make sure that they are the same as what you do today.

MS. RAND: Thank you. Damon Silvers.

MR. SILVERS: I just wanted to comment on the issue of whether or not material inconsistency and material misstatement of fact are necessarily a legal conclusion. I mean, I think that the issue that has been raised is an important one to get right. But that without a statement about scienter here, it's not a legal conclusion, at least with respect to 10b-5. And I can't see how you could even -- I can't see, if an auditor were aware of a material misstatement of fact under the current reporting rules, that an auditor could sign the letter certifying the financial statement.

So, it's not clear to me this even, at least as
stated on this slide, that it necessarily even represents an expansion of the auditor's current duties. And as long as you don't add a scienter component to it, I don't think it represents a legal conclusion.

MR. BAUMANN: Thanks, Damon. Wally Cooney.

MR. COONEY: Most of the concerns that I had have been covered one way or the other. So, I'll just comment that I share the concerns about the expectation gap. While it's helpful that the opinion drafted clearly says that they did not audit this other information, I think that's important, the word evaluate, even in the context of specific procedures, I think could really cause a problem with respect to expectation gap.

And just in practice, now that the auditors will be commenting, at least providing negative assurance, on the other information, I think sometimes that has the practical effect of just taking on a life of its own, including getting into non-financial information, and a lot of work, a lot of discussion, a lot of higher and more experienced people spending significant time on going through all that information. And I think there could be a significant cost effect.
The only other concern is that to the extent that MD&A is supposed to be through the eyes of management, it really is supposed to be management's report. I have some concern that companies may want to limit disclosure, maybe water down some of the commentary that they might have otherwise felt was more transparent and comfortable saying, but not having it subjected to the scrutiny of a long, drawn-out review process and discussion.

MS. RAND: Thank you. Professor Cox?

MR. COX: I think it would be helpful if you could separate these two issues out into two things. One is the process. Exactly what are the documents that are to be looked at and what the procedures are to be by the outside auditors, what they are supposed to look at, in which they are going to formulate some sort of opinion.

And then the other question I would say, separate from that, is how and to whom you communicate that. Richard Breeden made the observation, and never underestimate the power of a modifier: appropriate. And I think that that's something worth thinking about.

But the other idea I would put out there to take also some of the steam out of the process and some of the angst
out of the process, is to work this a little bit through the existing legal framework and think that maybe investors are not the group. That a big full-blown evaluation or reporting on the evaluation to all the investor community is not where you want to go. You would say add to your standard that conversations have been had. That your duties are to see if there are any apparent inconsistencies, and part of your obligation is to communicate those to the audit committee. In which case I would think that that then triggers the existing format for what happens to auditors in certain situations under 10(A) of the Exchange Act.

And that could be a way of at least making this initial step. I'm not sure where we are going to be ten years from now in terms of this process, but maybe this would be a somewhat more palatable process to going through.

But I do think it is going to be useful to you to unpack, first of all, what you want the auditors to do from the question about how that then gets communicated and to whom.

MS. RAND: Thank you. We have talked, just reflecting on the comments so far on this subject, talked a lot about the procedures, what does read and evaluate
mean, the work effort. I haven't heard that much, though, on the point regarding usefulness of reporting.

In our outreach we had heard, in one of the alternatives presented in the concept release on whether or not the auditors should provide additional assurance, was not to provide additional assurance, was really just describe the responsibilities that the auditor does with respect to the annual report. So, that was our intent. It initiated from a reporting element, thinking that might be useful.

So, I'm interested in feedback on that. We did feel that the current version of the report, just the read and consider with no procedures, wasn't robust enough to support a reporting statement in the auditor's report. So, we felt we needed to make some enhancement, have some minimum set of procedures regarding what the auditor does, their procedures over the other information.

But interested very much in is having the auditor report on, whether it's consideration, evaluation, is it used in the auditor's findings, is that useful to investors. So, hopefully, any other comments or if anyone that has their comment cards up now has any reaction, I am interested
in thoughts on that.

Next, is Gaylen Hansen.

MR. HANSEN: Jennifer, I absolutely think that it would be helpful to clarify this aspect of what auditors do. And I agree with what has been said. A lot is done now, and I think that what you have done here is responsive in large part to addressing that issue.

I will try to bring out just a couple of other things really quickly, though. Who does this? And it's not the firm. It's people within the firm. And I think for it to be meaningful it needs to be senior individuals on the engagement team. And all too often I have seen this delegated to lower level staff people.

And that tends to be a focus on the numerical aspects, as opposed to the qualitative, the nuance, and the spin and the tone. You read the financial statements and they have one tone. And you read the forepart of the 10-K and it is almost a completely -- it seems like it's written from a completely different perspective. And particularly when it comes to minimization and exaggeration and the wording in which you couch certain things I think does impact the way investors might approach things and consider
To your example, making widgets and characterizing yourself as the leading manufacturer of the widgets when you know you are the third, well, a lot of times what I see is someone saying we are a leading manufacturer of the widget. And you know perfectly well that's not the case. It's a misstatement but it's not numerical. And for a lower level staff person to be able to pick up on that, I think, is asking a lot of them.

So, I think that who does this and the tone and the spin and focusing on the qualitative is just as important as the numerical.

MS. RAND: Thanks, Gaylen.

Steve Buller.

MR. BULLER: Thank you. First of all, just a couple clarifying comments. One is I thought there was the inference earlier that a material misstatement may be fraud. And, certainly, there are conditions where you may have errors or typographical issues that of course, you know, occur. And as long as there is not intent or knowledge of the misstatement, I don't think, as a non-attorney, that would be something I would classify as
fraud.

And secondly is with respect to just the timing of press releases and 10-Ks. There are some companies that do produce a 10-K and a press release concurrently, but quite often it is because they material information that they need. Quite often it is codependent upon a third party and they can't obtain that in time to provide an earlier press release. But most companies do a press release two to three weeks after quarter-end or period-end. And so that does proceed to 10-K in most situations.

But they do, of course, make sure the information that is in the press release is, in fact, accurate because most of it does, as you said, Marty, appear in the 10-K.

So, the main question is we do support clarifying the responsibility for other information. I think it's a good idea. I think, generally, I am concerned it could be an expansion of scope, especially if the other information includes documents that are incorporated by reference. I know when I go through our 10-K and through others, incorporated by reference documents often are two or three pages long of listings. And our concern, of course, is that it would take auditors just time to read that listing, let
alone to read the documents that are included in there, just
to see if there is information that may in fact be relevant
to the audit.

Then, lastly, is I think that as part of the auditor
performing their work, even though I know they are supposed
to consider and evaluate information that's based upon
evidence that has already been obtained. If I were an
auditor and I saw, for example, information that had a
number of factors, one of which was information that was
based upon audit information that I had obtained to do my
core financial statements, but there was other information
I had not obtained, or did not have, I would make sure my
audit planning included getting that information as part
of my audit.

So it may in fact be that there would be an expansion
of the scope just to CYA, in part, to make sure that where
there is information presented with information that would
not otherwise -- would only be obtained as part of an audit
that now becomes part of the audit planning process and
therefore is obtained as part of the audit.

So, again, it's probably just the discussion of the
expansion of scope. Thank you.
MS. RAND: Okay, thank you, Steve. Elizabeth Mooney.

MS. MOONEY: Okay, thanks. I think it would be great if the earnings release and the 10-Qs would come out at the same time. That would be fantastic. And some companies do do that.

Obviously, investors do respond. Marty, just to echo your comments, I mean, they do respond to the most recent information, whatever that is, and the earnings release is significant.

But my experience, I had the great fortune of working with the best and brightest. I believe, investors, analysts, and for the long-term, fundamental research is all we do. And they do read the 10-Qs extensively and the 10-Ks.

So, I think, in terms of the other information, I said this earlier, but the goal, and we're getting a little sidetracked with a lot of this, but the goal is if the auditors are aware in their work of material misstatements otherwise, like Gaylen mentioned, that there is some responsibility to fix it.

I mean, I think that's the end goal and not just be
silent. And I think that is the spirit of the project and
just I would encourage you not to lose sight of that.


MR. MURRAY: Jennifer, a question, and a brief
explanation of why I ask. The question is is it correct to
understand that if the additional information that's at
issue is itself not material, then it is impossible for that
information to produce a material inconsistency or a
material misstatement?

And the reason for the question has to do with the
rapidly emerging movement now called integrated reporting,
which really has two prongs. One of which is the view of
many, that there should be more attention to
sustainability-related information included in financial
reporting as a voluntary, non-material election by
reporting entities. And the second prong, best
illustrated by the work of the Sustainability Accounting
Standards Board, suggests that all sustainability-related
information should in fact be recognized as material.
And it's that duality of position at the moment, and
what will be, I think, a very rapid evolution to
sustainability reporting issues arising in the next few
years, that I direct the question. Because those issues
would be a great deal easier to deal with if there were two
points of clarity. One is the answer to my question and the
other is what standard of materiality will be applied in
making the determination of what falls within the scope.

MR. BAUMANN: I don't think I have an answer to your
first question, whether or not one could conclude that if
there is no other -- if the information by itself is not
material, could you have a material misstatement or a
material inconsistency.

There is requirements of what has to be included in
a 10-K under the Securities Act. And I don't think we've
thought through whether that information, or some of that,
is by definition not material and therefore it wouldn't be
subject to a consideration of a material inconsistency or
material misstatement of fact, or whether a company decided
to put in other sustainability information and how that
might fit into this equation.

I think you've raised some things for us to think
about with respect to that, but I don't think we have really
explored that thought as part of this proposal. So, I will
just say we will take your comment and note it and give it
some thought.

MS. RAND: Okay, Wayne Kolins.

MR. KOLINS: Yeah, thank you. With respect to the reporting and the relationship of that to the limited nature of the procedures. And the procedures are more than read and consider and probably is similar to what is done currently in practice. But the conclusion is the negative assurance that was mentioned before is something that you see in a review engagement.

These are not review procedures. I think they are probably something less than review procedures. And I wonder if a way around that would be to specify that these are limited procedures, describe what the auditor's responsibility is to see that the information is revised, and if it's not, to refer to it in his or her report. And the absence of any such revision would be implicitly that they auditor did not have an issue with it. That the auditor did not become aware of anything.

Just an approach to take care of the very limited nature of the procedures and the ultimate reporting on it.

MR. BAUMANN: We understand that point and understand the careful line between the nature of the type
of assurance being expressed and whether or not the
procedures are the right procedures in connection with that
type of assurance.

So, we gave a lot of thought to that in putting this
out, but we'll continue to do that based upon those kind
of comments. Thank you.

Who was next? Bill Platt.

MR. PLATT:  Thanks, Marty. Just as I listened to
the discussion, I sort of have two observations around this.
And this is one area of the proposal that we spent a lot
of time thinking about.

One is the performance of the work. And I think
largely I would say that the procedures that are laid out
in paragraph four may in fact be fairly consistent with what
people are doing today in read and consider for a portion
of the other information.

And when I say that, you really think about the other
information. There is other information that is derived
from the company's accounting records, was subject to the
company's internal controls, and has been the subject
matter of the audit. The audit tests have been performed
around it. But then there is other information that is not
related at all to the company's accounting systems or systems of internal accounting control.

And I do think that in 4(C), I think, would be this characterization of other information not directly related to the financial statements. I don't know that it is clear enough for me to know what I would do as an auditor to that information.

And right now you sort of would say, well, if an underwriter asked me for comfort and started circling a bunch of items for me to give comfort on, I would give comfort on the items that are derived from the accounting records or subject to the internal accounting control, but I would say that the other information is outside the scope of my audit, it's outside of the areas of my expertise and I wouldn't give comfort on it.

So, I guess I worry a little bit about this other information and what the expectations are and are we changing kind of the performance expectations or standards around that information. And if we are, I think we need to be clearer than this simple reference that's in 4(C) right now. So, that would be the performance side of it.

The other side that I had is in the reporting now
of what's been done. And we are creating maybe a new
byproduct level of service called an evaluation. We
evaluate it. And, to me, I think evaluation implies
something more than I considered in relation to the
information that I had as an auditor. And I wonder whether
or not the report is actually being set up in a way that
will create an expectation gap, notwithstanding what the
standard requires, which is consideration of consistency,
but evaluation getting to a point that one would say, well,
that to evaluate then you just have drawn a conclusion,
which might then go beyond and actually start having
piecemeal opinions on pieces of information that are in the
other.

And this might go a little bit to Rick's question
about immaterial information. Say you had a $10 billion
company that had no real estate at all, 10,000 square feet
of office, it just happens to be a very virtual company,
and it was misstated by 2,000 square feet. It's material
to the square footage of office space but is it material
to an investor as you sort of look at that?

So I think some of those questions about materiality
may actually come into play here if there's going to be an
explicit statement that there wasn't an identification of
a material misstatement.

So, I think that those would be my two places that
I would suggest further thought around. One, is what do we
need to do around information that's not from the either
accounting records or subject to the system of internal
tools over financial reporting? And, secondly, to make
sure that we don't create a reporting format that is
creating an expectations gap but truly is providing
informative information to users of financials.

MS. RAND: Bill, do you have the paragraph 4(C)
which you referenced, which is other information not
directly related to the financial statements? That could
be the example I gave about the leading manufacturer of
widgets and the company purports to be that but you know
that they are not. They are the third.

MR. PLATT: So, what if --

MS. RAND: Do you have a view as far as should the
auditor ignore that or, you know, kind of what should the
responsibility be?

MR. PLATT: But what if we have two auditors that
one happens to know that and the other doesn't? Is the
inference that you always should know that? And what happens if, for example, there is a lot of different ways to measure leading?

So, they manufacture more widgets than anyone else in the world from a unit perspective but they are the third in revenue because they manufacture cheap widgets and other people manufacture premium widgets. Is that something that is a material misstatement of fact or not? There are two leaders, depending on what metric you use, if you use total revenue or you use total units.

I think it introduces a lot of interesting concepts. And I also don't know -- I mean, I might think that I know that they're third, but I really don't know from my audit. I only know from other public information that's out there that everybody else can see, too.

So, I think even though you have a simple example, I'm not sure it as simple in the real world when you really try to apply it.

MS. RAND: So I'm assuming, and I'm not sure if it's a correct assumption, that you may be more supportive of the responsibility today, just if the auditor becomes aware of something. But I think what I'm hearing is you are
concerned about the reporting on that aspect, the material
misstatement fact.

MR. PLATT: Or the pieces that go -- for the pieces
of information that are not derived from accounting records
or subject to internal controls. I think I would say yes.

MR. BAUMANN: So, of course, we do say -- so, these
are in context of you should read this other information
and, based on relevant audit evidence obtained and
conclusions reached during the audit, evaluate things.

So, it's not requiring you to evaluate that other
information not directly related to the systems, based upon
some new procedures. It's whether or not, when you were
reading the minute, understanding the company and its
environment, as part of those risk assessment procedures,
you became aware of aspects of the company and their
position in the marketplace, et cetera, or the growth
opportunities or other things that when you finally read
the other information, based only on procedures you
performed during the audit, the risk assessment procedures
and all of that, you became aware of it.

So, we do have that limiting factor. It may not
ameliorate your concern but that was the intent of those
words. You don't perform additional procedures. It's based on what you know.

So, the answer to your question would be one auditor might know with respect to a statement management makes that that is an inconsistency or a misstatement of fact, and another auditor might not know that because they didn't come upon that in their risk assessment procedures. So, that is a possibility, because it would be based upon what you learned as part of risk assessment. So, that is a possibility.

But the other point, I think, and you've made a lot of good points there, Bill, is there is different ways to understand leading. We just hope that that would trigger a conversation. If the auditor thought there was a misstatement, it doesn't mean the auditor is going to report that. We just hope that would trigger a discussion. And I would hope it would trigger a discussion between the auditor and management about let me understand the context in which you've said that. I thought I understood something different. And maybe it would trigger a conversation. If that wasn't satisfying with the audit committee, et cetera. But hopefully that would be resolved
before somebody reported something.

MR. PLATT: Yeah, and I think those conversations largely take place today, Marty.

Just on the point of the other information, though, you know, and I think sometimes, in terms of a layman, and to say that there is other information that I don't have anything in my knowledge base to know anything about and therefore I say, well, I don't know whether it's true or not true but because I don't have any information from my audit to evaluate it, I'm going to be okay it. And then to characterize that as you have evaluated, it seems to me it may be setting up what I described before as that expectation gap. It's sort of odd to say that is an evaluation just because you didn't know anything.

MR. BAUMANN: I completely understand your point.

Thanks.

MS. RAND: Okay, Dan Montgomery.

MR. MONTGOMERY: Thank you, Jennifer. And just getting back to your earlier point on just some input on the usefulness of reporting on other information, and just to give a little bit of international perspective on that. The IAASB did consider the alternative of simply
acknowledging in the auditor's report the auditor's responsibility for reading the other information, reading and consider, reading and evaluate, whatever the terminology, and perhaps indicating a responsibility to discuss any issues identified with the audit committee.

But the IAASB heard very strongly through two public consultations, three public roundtables, and a significant amount of outreach that there is value to an affirmative statement by the auditor in the auditor's report on the auditor's responsibility for other information and the outcome of the auditor's work effort.

So, just the point in terms of usefulness, the IAASB is firmly committed to moving forward with an affirmative statement on other information in the auditor's report. This was something that was supported not only by investors, but there was strong support from regulators, from national standard setters and from other stakeholders globally to move forward because of the value of that statement in their view.

However, I also would point out that the IAASB will continue to look at the wording of the reporting language so as to not create any confusion or misunderstanding or
certainly not further expand the expectation gap, and will be doing so in connection with its further work on finalizing the revision to the IAASB other's information standard, ISA-720.

MS. RAND: Thank you, Dan. That's helpful.

I see a couple of other cards up and I don't know if they're just up from previously: Steve Buller and Wally Cooney. Okay.

I have according to my watch that it's 10:30, which is break time. We've got a 30-minute break scheduled. I wanted to see if there was interest, anybody had any other topics -- I see one card up -- on other matters. So I see a couple. I would like to take those because I think, even if we have a little bit shorter break, we would still be okay. So Mike Cook?

MR. COOK: Thank you, Jennifer. I just have a sort of overall observation about a lot of the things that have been talked about, sort of the question you haven't asked. And I guess I think it's okay to answer it if you didn't ask it, but it's not a definitive answer. But one of the questions to me, an important question, is cost-benefit. What are the costs that we're going to impose by whatever
we end up doing? And what are the benefits going to be? I know the economists get involved, and a lot of other people get involved in that. But that is a very important issue. So I'd like to take the opportunity to comment on that.

Many of the people who offer comments say, "I appreciate the opportunity to talk about this subject." I have talked about this subject, the auditor's report, for so long I don't know for sure that I appreciate the opportunity anymore, but that doesn't keep me from offering a few thoughts.

And then I would like to give you one suggestion from the perspective of an audit committee chairman that might really produce a benefit with whatever you ultimately decide to do. And I'll save that for the last.

As I look at the cost-benefit of this, like a lot of things, the costs are more obvious than the benefits. If you accept, this will make investors better informed as an overriding consideration that drowns out any cost issues. You can get to that answer pretty quickly. I don't think of it that way, and I don't get to that point. But for me, the cost, the dollar cost, of implementing what we have here or some modified version of that is going to
be significant. So the benefit has to be significant, and
I can't quantify either one of those for you.

We will divert audit attention from things that
matter in terms of audit quality. We may do it depending
on how this gets implemented at a time of the year after
the end of the year when we need all of the attention we
can get to the critical things that need to be done to
complete an audit. And doing this, critical audit matters,
writing them up, getting them reviewed, talking to 14
different people, I don't think is going to meet a standard
of adding to audit quality.

I think there is a real risk of obscuring the key
messages that do need to be delivered. I happen to like the
pass/fail. I don't think we are abandoning that. But if
you have a hard time finding it or when you find it, you
are not sure that you did pass because you got so many other
things in there that might indicate that you really didn't
or you barely passed, I think that is a serious issue.

I am quite concerned about the issue of original
reporting, auditors reporting things that are not being
reported through management, through the financial
statement process. I am very concerned about some of the
discussion about disclosure and essentially creating new
disclosure standards through a requirement here, such as
with respect to material weaknesses and significant
deficiencies. I don't think that it is in the prerogative
or the parameters of the PCAOB to be writing disclosure
standards indirectly.

So I would point all of those things out as being
costs that are of concern to me. Then I get the benefit.
And I'll make a prediction, which I can't substantiate, but
I think a lot of people might see it the same way. And I
have heard it described.

I will predict that this will become lawyerized
boilerplate. And what we are trying to achieve, like a free
hand where the auditor gets to sit down and write how they
did the audit of company X and what bothered them in doing
that, will be totally overtaken by the need for uniformity,
legal considerations. And what we will see two or three or
five years from now, when we look at it, is going to be
boilerplate that is not particularly informative. I might
be wrong. That is my opinion of the way this will play out.

And I then put all of those points together and say,
does it meet the cost-benefit test for you? For me, it does
not. And so I just offer that. It's not quantitative conclusion. But I think the need to step back and really ask what costs we're imposing, financial costs and diversion costs and unnecessary information costs, the kitchen sink that we're going to get, which I happen to agree with, when you start adding all of those up, the benefits have got to be very clear and very direct.

I also would observe, however, that I think this train has left the station, meaning I think I've heard it said often enough in the last day or so "We have to do something." I'm not compelled to conclude that we have to do something if we're not doing something that meets the cost-benefit test and is the right thing to do. But there apparently is a conclusion that we've got to do something here. So if you have to do something, then I would just say, you know, think carefully about the implications of what you're doing.

This last discussion about other information is very much on point, I think, with that issue. I didn't really want to get into it because it was being well-said by others. But the word "leading" is not a fact. And if you're leading people, using that word, into challenging
that as a statement of fact, there are many accounting firms in the United States who claim to be the leading firm. That is not a statement of fact. Largest is a statement of fact. That is quantitative and could be challenged. It is just an indication of the areas that you can be leading people into that are going to be very problematic. And I like to know about these things as an audit committee chairman.

I would like to go to one other phrase that is used by members of the Board and others. I want to know what keeps the auditors up at night. And this is now my request to you. As an audit committee chairman, I want to know what keeps the auditors up at night, but I don't want to find it out next February or next March. This is my standard pitch. I'm not going to give you the big story about timeliness. And for the auditors to be writing next February or March about what kept them up at night in this year, when it's relevant to know that, from an audit committee standpoint is not satisfactory.

So I would urge you please if you are going to go forward with this, either in this standard or by rewriting or amending the standard on required communications with audit committees provide for this information to be given
to the auditing committee on a timely basis. I want to know
today what is keeping the auditors up at night. I hope they
don't have anything like that, but I really am not
interested in finding that out next March. And I represent
the investors in our company. And I need to know that
information now. And I don't see any reason why you can't
build a requirement to that effect into whatever
conclusions are reached about critical audit matters, but
timeliness is very important.

Thanks for the opportunity.

MR. BAUMANN: Thanks, Mike.

Obviously we will clearly explore the economic
rationale behind all of this. We have done that and
discussed that to some degree in the proposal itself and
certainly as we think about next steps, whether it's a group
proposal or adoption, we'll clearly have to articulate the
economic rationale of the need for this, various
alternatives you may have considered to solve whatever the
need is and, you know, what are the costs and related
benefits. So that is something that's, without a doubt,
things that will -- we will definitely do that. And
whatever we ultimately issue and adopt will certainly
reflect a very thoughtful economic rationale behind it. That's part of our mantra to do that.

I don't want to cover too many -- you made a lot of good points. And certainly we'll think about all of them. To your point about hopefully no auditors would keep this from the audit committee until the time of the annual report being issued and the opinion, AS 16 has in it already the communications with audit committees a statement that communications with the audit committee should be done on a timely basis. We can always think of reemphasizing that and making requirements in a different way to ensure that they are timely if that is not occurring, but that is certainly built into AS 16. So this in no way contemplates that the audit committees wouldn't hear about the issues that keep an auditor up at night on anything other than a timely basis.

But thanks for the comments. They are the valuable things for us to think about.

MS. RAND: Okay. I see three cards up. So I'll take those, and then we'll go to break. So Bob Hirth?

MR. HIRTH: Thanks, Jennifer.

I had one comment on critical audit matters from
yesterday. In the draft standard on page A1-8, item 10, it talks about when financial statements are presented on a comparative basis and talks about where critical audit matters from the prior period might be restated. It talks about for the first time that information is presented publicly and also where there's a prior period where the auditor's report could no longer be relied upon.

I think what is missing there and I think you might add as a third point, where there are meaningful or significant differences in critical audit matters between reporting periods. What I mean by that is financial statements are generally presented in pairs.

And if you only have the critical audit matters of the most recent opinion, you're going to ask me to go back and find last year's opinion, which was the current year's opinion, and look at those critical audit matters. So if I had five critical audit matters that were exactly the same between both years, fine. What if I had five in one year and six in the previous year or five and some of them were different? So I think you need to ask the question, where you have that, should that be considered in the standard?

My second point was we've had a great discussion
over the last two days. And this is a really, really
important change. And, to Mike's point I think on the costs
and benefits, I would really encourage the Board to think
about how you monitor this with, you know, multiple parties
but clearly the investors, the filers, and the audit
committees, and get some feedback but also think about
whether or not this is so important that we go back and
report back to the SAG in a year or two on what the findings
were from those studies on the costs and the benefits
because this could be a standard that either continues or
gets revised or when you really sit down and look at it and
look at all of the benefits, you know, they weren't there
and that becomes superseded in some way.

MS. RAND: Thank you, Bob.

Elizabeth? Oh, go ahead.

MR. BAUMANN: Just one comment to Bob's. And that
is we have already announced that after the comment period
is over, which is December 11th, we'll analyze those
comments. And they certainly have a SAG meeting next May,
but we also have already announced that we plan to hold a
roundtable, some type of forum to discuss the comments that
were received and a focused meeting just on the auditor
reporting model as well as probably a SAG discussion in May. So we intend to get continued outreach and reaction beyond the many comment letters we get to make sure that we get all of that kind of input you're talking about.

So those are valuable points, Bob, and we plan to do that.

MR. HIRTH: And maybe just one step further. So would the idea be because we have these different parties that have, you know, different viewpoints? Would you even think about seeing that a third party does some kind of study or engaging some third party to really look at the costs and the benefits, you know, a year out or two years out or three years out?

MR. BAUMANN: Well, as Jim mentioned yesterday -- well, first of all, we have economists on board. And we'll be thinking, as I clearly stated, I hope, that nothing would go forward until we did a thorough economic analysis of why we're doing what we're doing, what's the problem we're trying to solve, and making sure that we're solving it in an economical way.

But we're also building the capability in the Center for Economic Analysis at the PCAOB to look at ways in which
after we issue standards, the effectiveness of the standards and the benefits of the standard vis-à-vis the cost. So we want to continue to build that capability at the Board.

So thanks a lot.

MS. RAND: Elizabeth, I had you next on my list.

MS. MOONEY: Yes. Okay. Thanks. I just wanted to go back to the point I made earlier just about the critical accounting matters and encourage you to be clear in defining that and use the existing standard that is required. So auditors should report the matters that are significant in accordance with the accounting rule. So it's already defined in the documentation standard. And that should be -- you know, so going back over what work has already been done, what has already been identified as significant, and then talking about that. Rather than introducing a significant amount of additional unnecessary judgment, we have, you know, lots of different perspectives, even in just this room.

And I think, with all due respect to, you know, auditors having lots of different views, I think if you introduce that into this, then it is just going to be a huge
loophole that is unnecessary.

MS. RAND: I am not sure I fully understand your point because you made reference to the documentation standards. So in my mind, I was thinking about the engagement completion document, which auditors document significant issues and findings --

MS. MOONEY: Right.

MS. RAND: And in developing the proposed auditing standard, it would have the auditor look to that engagement completion memo, the matters discussed with the audit committee, any matters communicated to or reviewed by the engagement quality reviewer. And then we have a definition of critical audit matters, which would be helping the auditor to identify not that entire population but those that are most significant to be communicated to investors in the report, rather than have a lengthy list of everything that might have otherwise been communicated.

So I wasn't clear on if you're thinking that our definition as proposed may be sufficient for purposes of communication or if you're --

MS. MOONEY: No. I think the proposed definition is insufficient because it doesn't -- it should say, I
believe, that what should be reported is what is significant
in accordance with the current standards, now, not
everything but the completion engagement memo to the extent
that that talks about what is most important.


And Arch?

MR. BAUMANN: Final word.

MR. ARCHAMBAULT: Thanks, Jennifer. There was an
item on the slides yesterday we didn't get a chance to talk
about in detail. And that is the documentation. And there
was an aspect of that. And, again, my firm is still in the
process of developing our letter, but one thing I have
raised in connection with this documentation is that it
seems like an extremely onerous requirement to document not
only those matters that you have identified and believe are
critical audit matters but those, and I think the words are,
that appear to be a critical audit matter but are not treated
as one. So you're trying to document the negative. And
the current documentation standard of the Board in my view
is very robust.

I am not aware of anything where we have to document
the negative. In other words, we will do a risk assessment.
We document those areas that we feel have a higher risk of material misstatement. We have to document how we respond to those risks. We don't have to document those areas that we don't feel have a higher risk of material misstatement. And that's what this standard is directing us to do from the way I read it. And to me, that is going to lead to a situation where I think auditors are going to get extremely cautious to avoid any second guessing.

So I ask you to take a careful look at that and really decide whether that kind of a requirement is necessary here.

MS. RAND: I am glad you raised the documentation requirement. In developing that requirement, we considered whether it should just be only document those in your work papers, where the auditor did report a critical audit matter.

Our concern was the determination of critical audit matters is judgmental. It's those that were most difficult in forming the opinion, most difficult obtaining evidence, just had subjectivity and difficulty. So that determination is judgmental. And so if the auditor just determines, leaves something critical off, then what would be the safeguard to prevent a matter from appearing in the
We thought that if there is an issue that would appear to an engagement quality reviewer, that would otherwise appear, which is an experienced auditor, to have met their criteria, then that would be -- and was not communicated in the report, then that matter or matters should be documented so that the engagement quality reviewer would understand the rationale.

So we thought having that, kind of requiring the auditor to document it, it may have been something that was discussed significant with the audit committee that an experienced auditor would otherwise say. That should have been in the report. Why wasn't it? We felt that was a safeguard. We didn't think that the nature of the list would be extensive in our view.

And I know Marty is jumping up. So I don't know if you have anything further to add.

MR. BAUMANN: Well, I just want to -- you raised a very good point. And we expected to hear commentary on that. So we're glad you brought it up. And I'm sure it's going to be in the letters.

I think Elizabeth's point was require specific
things to be reported and have what's reported as critical audit matters based upon specific things that are mandated in our standards that you have to report on all of these things in the audit report. And that's one way to go. And so her comment was standards-based, write rules, pretty much like AS-16, communications with audit committees, take a subset of that, and say these have to be communicated in the audit report. Then that's one route to go.

The other route was the way we went, which was what was in the auditor's view the most difficult, subjective matters that he or she faced. But the problem with that was that there is a risk that Jennifer pointed out. What is the safeguard that the auditor will not under pressure or whatever, decide that I'm not going to put this matter in because management and the audit committee don't really want me to. What is the safeguard around that risk?

And so we had to think about that risk, that that could occur. And, therefore, maybe a documentation standard, something that might appear to an experienced auditor, to meet this, the standard, has to be documented.

So we understand your point, that it gets to whether
or not we keep this as a judgmental based upon what the auditor believes are the most difficult matters to be reported or really change our threshold to say it is mandated that these items have to be reported and go to what Elizabeth said. Just put it in the standards, "This has to be reported in the audit report."

So that is a threshold decision for us. And the way we put it out in the proposal was one way, but based on comments, we'll reflect on maybe what some others have said. Do this according to standards and rules.