

NOTICE: This is an unofficial transcript of the portion of the Public Company Accounting Oversight Board's Standing Advisory Group meeting on May 15, 2013 that relates to the Board's proposal on improving transparency through disclosure of engagement partner and certain other participants in audits. The other topics discussed during the May 15, 2013 meeting are not included in this transcript excerpt.

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15 The next one, No. 5, I want to talk about with
16 No. 8, which is identification of the engagement partner
17 and identification of other firms participating in the
18 audit. We've proposed this initially as -- well, we had
19 a concept release on whether or not the engagement
20 partners should sign the audit report. And then we put
21 out a proposal of identifying the engagement partner in
22 the report, and in that proposal also identifying other

1 firms that participate in the audit.

2 The nature of some of the comments we got back on
3 the two different issues were different, so we decided
4 to separate them, but we continue to think about them as
5 whether or not we should, if we adopt this, adopt it as
6 one item. Jim spent a lot of time on this. I won't
7 spend too much more, but there is a great demand for
8 investors to know who is the audit partner who had
9 primary responsibility for this audit?

10 The audit partner is identified in many countries
11 around the world. It's becoming increasingly common
12 throughout the European Union, Australia, other places.
13 Investors in the United States want that information.
14 And that information can be very valuable over time, just
15 like knowing which firm did the audit; and different
16 firms have different audit quality; knowing which partner
17 led the audit; and different partners have different
18 skills; investors think has great value. In addition to
19 that, academic research has indicated the identification
20 of the name of the partner in the audit report could
21 increase the accountability of that engagement partner
22 in the performance of his or her procedures.

1 Right now, as noted in our inspection reports --
2 and I was reading today the Australian ASIC, their
3 inspector was saying that in 20 percent of their audits
4 they're finding deficiencies. I don't know the exact
5 percentage off-hand in our audits, but it's potentially
6 possibly around 20 percent of the audits that we inspect
7 are not up to PCAOB standards. If auditors felt more
8 accountable by having their name identified in the
9 report, hopefully that number would decrease greatly.
10 So we think that's a very important aspect.

11 Also, knowing what other firms participated in
12 the audit and the extent of their participation is very
13 important. There can be things as dramatic as some of
14 the reverse mergers that have taken place -- well, I'll
15 just use China as an example -- where an operating
16 company in an emerging market may have merged with a
17 shell company in the United States and there's an auditor
18 signing that report in the United States, but nobody
19 knows that 90 percent of the audit work, or 95 percent
20 of the audit work, is being performed by a firm in that
21 emerging market, or maybe that that firm is not inspected
22 by the PCAOB because the PCAOB can't inspect in that

1 country.

2 So identifying other participants and their
3 extent of participation, I think, is very important, not
4 just in those scenarios, but also in many U.S.
5 multinationals. A great extent of the audit, it could
6 be 60 or 70 percent of an audit, can be done in other
7 countries by other auditors. Some of those countries we
8 can inspect in. Maybe some we can't. Even if we can,
9 the different firms that are involved in the audit may
10 have very different inspection reports with respect to
11 the quality of their work.

12 In any event, we think all of that is very
13 valuable to investors. So we are moving forward with
14 improving the transparency of who does the audit, both
15 the engagement partner and other firms employed in the
16 audit.

17 Denny Beresford?

18 MR. BERESFORD: I guess first a question. From
19 both yours and Jim's comments earlier, do I gather that
20 this is going to be a final statement as opposed to a re-
21 exposure?

22 MR. BAUMANN: We are working our way through it.

1 And a lot of important issues were raised by commenters,
2 including questions around if we're identified does that
3 trigger consent issues? And if there are consent issues,
4 does that trigger additional liability issues? And we're
5 working our way through all of these issues ourselves.
6 In NOCA, with our Office of General Counsel, with the
7 Board. We're in active discussions with the SEC. We
8 have it on here as adoption or reproposal. And I think
9 the final decision on that will still have to be made.

10 MR. BERESFORD: Okay. The concern I have -- I
11 guess, really, it's hard to respond with just verbal
12 comments without seeing what you have in writing. When
13 you make the comment "great user demand," I know this was
14 in the earlier document as well, and then particularly
15 the comment about "academic research could increase the
16 accountability of the auditor," that's of some concern.
17 I guess almost anything could increase accountability.

18 This I know was a concern that some people had
19 expressed in both comments at SAG earlier and in comment
20 letters, that many people believe that the accountability
21 of auditors is pretty high now when they have to sign off
22 their responsibility statement in their firm's internal

1 documentation and so forth. And there are some who
2 assert that if their name is stated that they somehow or
3 another will have greater accountability.

4 I am not aware of the academic research that
5 indicates somehow or another that they could increase
6 accountability. That's something that I guess I would
7 be interested in seeing, not that I would necessarily be
8 qualified to judge that. But any time I hear terms like
9 "could increase accountability," I always get concerned
10 about that, Marty. Anything could do that.

11 But I remain concerned about the great user
12 demand for naming the audit partner and this notion that
13 somehow or another that the naming of the individual is
14 going to increase the accountability of the auditor.
15 Both of those assertions, particularly the latter, just
16 don't necessarily work for me completely.

17 MR. BAUMANN: Thanks, Denny. That's probably my
18 word, could increase accountability. I think some of the
19 academic research that we've seen, the academic would
20 probably take exception with me also and say that my
21 research has shown that it does increase accountability
22 if somebody is signing a document in their own name. So

1 that was probably my error in saying it could. But we
2 are carefully looking through research to identify
3 research on this subject, both directions, as we
4 carefully think through this issue.

5 Chairman Doty?

6 MR. BAUMANN: You yield to Elizabeth Mooney.

7 Okay. Elizabeth Mooney.

8 MS. MOONEY: Oh, I just briefly wanted to say,
9 you know, that this project is very encouraging. And
10 from my work with investors internally, they would really
11 welcome this information. Long overdue.

12 MR. BAUMANN: Thank you, Elizabeth. Jim?

13 CHAIRMAN DOTY: On the subject of the academic
14 research and the relationship between disclosure and
15 conduct, to partly address what Denny's concern is, there
16 has been a question of whether, in fact, disclosing this
17 information would make the partner more accountable.

18 In our formulation of this and our view of it,
19 this is a disclosure rule. The interesting thing about
20 the academic research, and if you look at what Ann
21 Vanstraelen at Maastricht and her colleagues at Florida
22 have done, they have situations in which you have a

1 continuous long record of identification of the
2 engagement partner. And the important thing about that
3 is that patterns of conduct, patterns of error, omission
4 and success by the engagement partner emerge over time,
5 just as they do with firms.

6 This is principally a disclosure rule. The
7 market wants to know whether, in fact, the partner that's
8 on their account is someone who has a long history of
9 bungling audits, restatements that have trailed or
10 followed him or her, or whether this auditor has a
11 history of making tough calls and being an objective
12 auditor.

13 All academic research, as Denny will I think
14 agree, all academic research has limitations. There are
15 limitations in the sample. There are limitations in the
16 location of the research. There are limitations in what
17 is available in the archival record. That said, I'd just
18 say it is an impressive piece of research on the patterns
19 of conduct in an area in which we are constantly told
20 this is a matter where judgment matters, judgment is
21 called into question, individual aptitude, individual
22 training, individual ethics all matter. And what

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1 Vanstraelen's research shows is that if you start
2 stretching this out over time, investors can go back and
3 can see where the behavioral patterns or the
4 qualifications of the auditor lie.

5 It is very hard for me to see why -- since in
6 much of the world the memory of man runneth not to the
7 contrary, to the point where investors didn't know their
8 engagement partner -- why would it be true that in the
9 United States of America in the 21st Century you don't
10 know the name of your engagement partner unless you go
11 to the annual meeting? If an investor in BNP Paribas has
12 not only the name but the signature, how can we possibly
13 go forward in a world where we know that emerging markets
14 have different cultural assumptions about what auditors
15 will, in fact, call or do to check the validity of audits
16 and not, as Marty said, know what percentage of our work
17 was performed by auditors in these other cultures?

18 It is at root a disclosure. It is a disclosure
19 principle. To the extent that anyone says, well, it will
20 mean that auditors have to do more work, it will affect
21 their conduct. What I was trying to say earlier is any
22 good disclosure rule has an indirect effect on conduct.

1 Our system has rested on the principle, the sunlight
2 principle that is so often cited, that generally the
3 effect of that disclosure, if it is an effect on conduct,
4 is beneficial. It's salutary. What drives this one is
5 it requires no new work by the auditor.

6 So I would cast it that way, Denny. I think we
7 do know that other people get it, that other people want
8 it, and that in societies and in nation states where it
9 has been made routinely available, there are meaningful
10 conclusions that can be drawn from it.

11 MR. BAUMANN: Thanks, Jim.

12 Bob, is your card up from before or again?

13 MR. GUIDO: It's new. Actually, Denny beat me to
14 it. And I've got a couple observations.

15 First, I like the idea of bifurcation of this
16 issue. I'm all for transparency, but I do think we're
17 mixing apples and oranges when we talk about signators
18 versus accountability of firms involved, especially if
19 the individual firm that we're talking about is outside
20 the scope of the quality control system of that firm on
21 a global basis. I think that's really important.

22 On the signator, that troubles me, because if

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1 we're talking about the competency of the audit partner's
2 sign-off, to me that is the audit committee's
3 responsibility to do their homework to really ensure
4 you've got the right partner and he or she has not got
5 a bunch of baggage in their background. That is the
6 accountability that's needed in the capital markets. I'm
7 not sure that additional sign-off of an individual in a
8 report means a lot. And, as Jim said, go to the annual
9 meeting if you want to know that person who has a chance
10 of maybe speaking at that meeting. But, more
11 importantly, be careful of unintended consequences with
12 this. I'm really concerned about that. Thank you.

13 MR. BAUMANN: Thanks, Bob. One of the things
14 that I think we ought to take into account is at meetings
15 like this we have the audit committee members, who are
16 some of the best audit committee members in the world,
17 and not all audit committee members of 11,000 public
18 companies are the same. And investors say they
19 appreciate the work greatly that the audit committee
20 does, as do we, but investors feel they need this
21 information. And not all audit committees apply equal
22 rigor around some of these things. But I understand your

1 comment.

2 Richard Breeden?

3 MR. BREEDEN: As a member of a variety of audit
4 committees over the years, I think all audit committees
5 are underappreciated for the immense amount of work they
6 do, but I just wanted to respectfully disagree with the
7 previous comment that the audit committees ought to do
8 all the investigative work and not ask for a simple
9 approach of disclosure of the name and a sign-off from
10 the audit partner. I think there are a number of
11 benefits that can flow from that. You've identified some
12 of them. I think particularly in some of the offshore
13 countries there is a benefit from -- having this
14 identification may give additional focus and stature and
15 a little leverage to the audit engagement partner inside
16 their firm, because they now have certain identification
17 and certain responsibilities as being disclosed directly
18 to investors. And if their firm is telling them or
19 pressuring them to do certain things for certain clients,
20 it may help that they are not nameless and faceless. And
21 it may give them a greater sense of the importance of
22 their individual accountability without actually changing

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1 liability. I think that's good.

2 And I just think it's very hard to argue that
3 something as simple as this identification can't be given
4 to investors without the world collapsing around us. Not
5 every investor will think it's relevant. Some investors
6 may be perfectly happy with the work their audit
7 committee may have done, but others may want to have it.
8 And why not err on the side of giving investors as much
9 relevant data as possible?

10 MR. BAUMANN: Thanks very much, Richard, for
11 those good comments.

12 Steve Buller?

13 MR. BULLER: Thanks, Marty. I don't want to beat
14 a dead horse here, but just a few thoughts. We talk
15 about who the users are of this information, and there
16 are multiple users. There is of course the regulator,
17 the PCAOB. And that information may be useful to them.
18 I'm not sure that disclosing the name of the auditor as
19 a public disclosure is the only way that the PCAOB can
20 get the information. There is a preparer, which is of
21 course the company and the audit committee, which I think
22 has a responsibility to understand who their auditor is

1 and their background. And again, I'm not sure that
2 public disclosure helps that.

3 What I focus on is information that is
4 actionable. And so we talk to our analysts and to our
5 people who vote proxies. We say is this information
6 actionable to you? So if you see an auditor name and the
7 auditor is associated with a past failure, would you vote
8 a proxy no or would you as an analyst fail to invest in
9 that company because an auditor is associated with a
10 failed audit in the past? And the answer probably is no.
11 What you look to to see is whether or not the firm has
12 adequate controls and procedures in place and look to the
13 integrity of management, but the name of the auditor
14 probably is not something that's going to impact your
15 ultimate decision.

16 MR. BAUMANN: Thanks, Steve. Well, you can see
17 this topic has engendered interest in our proposals any
18 time we bring it up in conversation, so we're continuing
19 to work deliberately on this project.

20 I'm not sure whose card was up over there. Oh,
21 Roman Weil. Okay.

22 MR. WEIL: I'm going to take 45 seconds to remind

1 Denny of an anecdote. Twenty years ago you were chairman
2 of the FASB and I was on the FASAC. And the FSAB members
3 were complaining that you weren't getting enough
4 information, feedback, thoughts from academics about
5 proposals, exposure drafts and so on. And I said to you
6 the way to get us to write you is to acknowledge our
7 names in the exposure draft. Instead of saying somebody
8 said X, Roman Weil said X. Bill Beaver said Y. And you
9 heard me and you didn't do it and we academics didn't
10 respond. All we have is our egos. If you don't stroke
11 our egos, we're not going to do the work. So there's no
12 empirical evidence here, but my belief is that if you put
13 somebody's name on a comment, they're going to be more
14 careful about the comment. Perhaps give them more.
15 Maybe that doesn't apply to auditors. Maybe it does.
16 So that's the end of the anecdote.

17 What I don't understand about this discussion is
18 how we can have an auditor who -- bumbling was the word
19 that I think Jim used in describing contents of research.
20 How does an accounting firm let somebody persist who's
21 got a record of bumbling? I would think that publicizing
22 the bumbling will make the auditor go away. No firm's

1 going to let that happen. So we're probably not going
2 to see a history of bumbling. We'll see a history of
3 people being taken off the audit. What I can't figure
4 out is why the bumbling persists even when it's secret.

5 MR. BAUMANN: Thanks for the anecdote and the
6 views.

7 I'm sorry, Jerry De St. Paer?

8 MR. DE ST. PAER: It seems to me that if the name
9 of the auditor is put into the report that people like
10 Roman will soon do academic research to do correlations
11 between restatements and so forth and names of people.
12 It will create a body of data. That body of data does
13 not exist at the moment. So if they're sitting on a
14 audit committee; I've been through this, as many people
15 here, in large companies a number of times, you know a
16 lot of information about the person. And if you're a big
17 client, you really have the resources to dig into that.
18 It seems to me if the body of data that research could
19 provide from this was available, that that would be an
20 additional tool that would be helpful to the audit
21 committee.

22 MR. BAUMANN: We agree with that. I think that

1 body of data is going to be developed over time. There
2 are probably plenty of companies that want to develop
3 that and think it can be useful to investors, audit
4 committees and others over time.

5 Jeff Mahoney and then Jennifer Paquette. And
6 then I'd like to move onto another topic.

7 MR. MAHONEY: Thank you, Marty. As you know this
8 was a recommendation of the Department of Treasury's
9 Advisory Committee on the auditor signature. There was
10 general support within that group from the user community
11 for this proposed change. But also one of the strongest
12 and most articulate supporters of this proposal was a
13 former auditor from one of the largest accounting firms.
14 He pushed very strongly for this to be a proposal of the
15 Committee.

16 MR. BAUMANN: All right. Thanks.

17 Jennifer Paquette. And it was pointed out to me
18 that I missed -- Damon had his card up, too. So
19 Jennifer, then Damon Silver. And then we'll move to the
20 next topic.

21 MS. PAQUETTE: Thank you. I just wanted to
22 circle back to the comment whether the release of the

1 name of the auditor in itself would be a value to
2 investors. And I think I'd like to highlight the fact
3 that investors are making decisions based on a mosaic of
4 information. And any one piece of information may not
5 be the determinant of a buyer/seller whole decision, but
6 what's the importance or value of any of those pieces of
7 information that formulates that eventual decision.

8 I think that having the name of the engagement
9 partner is important and I think it's a component that
10 investors should be allowed to consider, as well as
11 academics, to evaluate over periods of time. I think
12 it's not something to be discarded in that. It may not
13 impact one particular decision, but it is an important
14 component potentially for investors to make decisions
15 going forward.

16 MR. BAUMANN: Thank you, Jennifer.

17 Damon?

18 MR. SILVER: I just want to follow up on what
19 Jennifer just said and add to it that while this issue
20 is obviously part of a complex mosaic of information
21 involving buying and sell decisions, it is a central
22 piece of information around corporate governance for

1 long-term investors, and particularly for investors who
2 are asked to vote on the audit firm, as is the case
3 typically in medium to large-cap companies. I mean
4 obviously there are firms that do not ask investors to
5 do that, but almost everyone does.

6 And it's not clear to me, although it's never
7 been raised in this way -- but it's not clear to me that
8 given that the identity of the managing partner in an
9 audit is a known fact, although investors are entirely
10 complying with their fiduciary duties around voting on
11 the audit not knowing who that person is.

12 MR. BAUMANN: Thanks, Damon. And thanks,
13 everybody, for contributing to the ongoing dialogue
14 around disclosure of the engagement partner and other
15 firms.