

NOTICE: This is an unofficial transcript of the portion of the Public Company Accounting Oversight Board's Standing Advisory Group meeting on November 10, 2011 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 November 10, 2011 meeting are not included in this transcript excerpt.

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PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD
STANDING ADVISORY GROUP MEETING

Thursday, November 10, 2011

9:06 a.m.

1201 15th Street, N.W.
Washington, D.C.

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PARTICIPANTS

MARTIN BAUMANN	KIKO HARVEY
ARCH ARCHAMBAULT	STEPHEN HOMZA
MICHAEL AUERBACH	ANTHONY KENDALL
DENNY BERESFORD	WAYNE KOLINS
NERI BUKSPAN	LISA LINDSLEY
ELENA BOZHKOVA	JEFF MAHONEY
JOE CARCELLO	BILL PLATT
BRIAN CROTEAU	STEVE RAFFERTY
BOB DACEY	JENNIFER RAND
LEW FERGUSON	SAM RANZILLA
MIKE GALLAGHER	BARBARA ROPER
LIZ GANTNIER	KURT SCHACHT
DAN GOELZER	ARNOLD SCHILDER
HARRISON GREENE	SCOTT SHOWALTER
MICHAEL GURBUTT	DAMON SILVERS
ARNOLD HANISH	BRIAN SIPES
GAYLEN HANSEN	DAN SLACK
GAIL HANSON	LARRY SMITH
STEVE HARRIS	LYNN TURNER
MARY HARTMAN MORRIS	BARBARA VANICH

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PARTICIPANTS (CONTINUED)

JOHN WHITE

DENISE WRAY

MEGAN ZIETSMAN

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P R O C E E D I N G S

[9:06 a.m.]

MR. BAUMANN: Well, good morning,
everybody. Thanks for getting back here so
promptly today.

From our perspective, we thought
yesterday was an excellent day in terms of getting
input on very important matters to us. We hope
that everybody has come back with the same level of
energy and excitement and enthusiasm to continue
the dialogue with the same intensity we had
yesterday. So that, we really appreciated that.

Before I get started on today's program,
we didn't give -- allocate quite as much time at
the end of the day to the transparency project as
we had laid out on the agenda, given the timetable.

So I just wanted to make sure if anybody had
wanted to make any further statement on that and
didn't have a chance, we could certainly comment on
that.

Barbara?

MS. ROPER: Since I cut out early, I'd

1 just very quickly say I am particularly
2 enthusiastic about the proposal to include the
3 disclosure of the other firms that are involved in
4 the audits. I think that will be useful, valuable
5 information.

6 So, and I'll put something in writing
7 before the comment period is up. But, thanks.

8 MR. BAUMANN: Thank you.
9 Mike Gallagher?

10 MR. GALLAGHER: Marty, I'm not sure I
11 know what a better way to do it would be. But my
12 only concern around hours is that hours can be very
13 different in terms of the quality of the hours. We
14 talked about offshoring and so forth, and we're
15 going to be thinking a lot about what might an
16 alternate measure be.

17 And then the other thing was just the 3
18 percent. We just thought that was a little bit on
19 the low side, and we'll be thinking about that,
20 too, in terms of alternatives and responding.

21 MR. BAUMANN: Those are really both good
22 points. We picked a marker and asked people to

1 comment on that marker. We needed to have some
2 sort of a place where you'd cut it off, obviously,
3 but certainly looking for input on that.

4 And I recognize that some hours in
5 certain areas are higher risk and more quality
6 hours than other hours, but we'll look forward to
7 suggestions on other ways to measure participation
8 in the audit.

9 Well, this topic does have more interest.
10 Good. Bill Platt?

11 MR. PLATT: Hey, Marty, thanks.

12 And I agree with Mike's comments. I
13 guess just the other thing that we're thinking
14 about is that even if hours is a measure, is the
15 disclosure of the percentage for each firm really
16 something that's necessary? So, for example, in
17 the example, I think you have one that's 3 percent,
18 4 percent, and 5 percent. Does it really matter to
19 disclose the percentages exactly, or might there be
20 ways to bucket it?

21 For example, firms that play a
22 substantial role and list all of them without an

1 indication of where they are in severity and those
2 that -- others that are above a threshold, but
3 below substantial role. We haven't formed a view
4 yet, but those are some of the things we're
5 thinking about as we think about it.

6 MR. BAUMANN: Again, we're interested in
7 feedback on how to disclose the participation of
8 other firms. I think many want to see the listing
9 of those firms who played a role and want greater
10 information. And there can be other suggestions of
11 ways to try to combine them, but we're interested
12 in all views, obviously, on the proposal.

13 Joe Carcello?

14 MR. CARCELLO: Yes, I want to get maybe
15 some feedback from people from the firms. As we
16 were talking about this last night, one thought --
17 and I'd be interested in the firms' reaction to
18 this -- would be a higher threshold rather than 3
19 percent. Let's say 5 or 10. But a lower threshold
20 if the firm is in a country that's not subject to
21 inspection.

22 MR. GALLAGHER: Yes, Joe. I think that's

1 something to think about. I think because that
2 definitely gets to an issue I know is of concern to
3 investors. So we'll put that into our mix as we
4 think about the solution.

5 Again, my issue -- and it really came to
6 life when you guys were talking about offshoring,
7 and somebody mentioned the nature of those hours
8 were very nonjudgmental, very administerial, and
9 that's the way things work in our firm. And to
10 have those hours be viewed as an apples-to-apples
11 with the U.S., where you really do focus on the
12 areas that are just so much more judgmental and
13 more impactful and more important, that was an
14 issue.

15 But your point around bifurcating between
16 what's subject to inspections and not I think could
17 be a good screen as well.

18 MR. BAUMANN: Our goal, Joe, is to get
19 the most meaningful information to investors on
20 this in transparency. So these are all suggestions
21 that we'll look forward to seeing in the comment
22 letters.

1 I see I think it's Lynn Turner and Scott
2 Showalter.

3 MS. RAND: Regarding inspections or
4 countries where we haven't been able to inspect, if
5 that's the nature of the comments, I'd be
6 interested in further thoughts on when would that
7 go in? For example, we may get agreement today to
8 inspect, but that inspection may not be conducted
9 by us. So is it when the inspection report is
10 issued, when the country just says we would come
11 in?

12 When would that lower threshold for
13 disclosure, say, in that example, when do you think
14 that would be appropriate? When would it be
15 lifted? Those are other considerations to take in
16 mind.

17 And just also even inspections, we may
18 inspect, but that we could have significant
19 findings. So it's like you're qualifying just a
20 firm that we haven't been able to be inspected. It
21 could be the firm -- if we did, we wouldn't have
22 significant findings.

1 I don't know. Maybe we would. But, so
2 just a thought, you know, if that's kind of the
3 nature of the comments, we'd be interested in
4 further thoughts on that to help our thinking.

5 MR. TURNER: Marty, a couple thoughts.
6 First, on the signature, I think you have two
7 issues. One, you want to make sure that people
8 understand it's the firm, and you don't want to
9 lessen the role of the firm. But at the same time,
10 we all know that what makes an audit work or not is
11 really the audit partner and whether that audit
12 partner is staying on top of it.

13 And so, I would encourage you to go back
14 and rather than just disclosure have a signature or
15 something like the name of the firm by the name of
16 the partner then, and I think that would work, by
17 far and away, the best.

18 With respect to the discussion that just
19 ensued about the percentages and all, as I was
20 listening to it yesterday, I actually think your
21 notion of hours is very good. Because what I want
22 to know is who was doing the significant part of

1 the audits? And if someone did contribute a
2 significant number of hours, I would certainly want
3 to know that.

4 As the chair of an audit committee, we
5 were approached by our audit firm to outsource and
6 outsourced stuff to India. And in this case, it
7 was a mutual fund, and some of the outsourcing, as
8 I recall, was going to be pricing. So I don't
9 think it's all just subjective stuff that's going
10 overseas, and so I would want to know.

11 I don't know that I'd do just down to 3
12 percent. Three percent seems, just my gut
13 reaction, is awful small. I may raise that up
14 some. But on the other hand, 20 percent is
15 probably too high, and I do want to know who's
16 doing significant things.

17 And then, to the last point, I do want to
18 know if that audit firm doing a significant part
19 isn't subject to your inspections. And to
20 Jennifer's question, I'd probably put the cutoff at
21 the date or time that those firms agreed to subject
22 themselves to inspection, and audits before that

1 would have to have the disclosure.

2 Audits that would become subject to
3 inspection -- might not yet have been inspected,
4 but would be subject to inspections thereafter -- I
5 wouldn't subject to that disclosure. But I would
6 very much like to know how much of the audit is
7 done by a firm that has not been subjected to the
8 PCAOB inspection process. That's very important to
9 me.

10 MR. BAUMANN: Good. Thanks, Lynn.

11 And Scott?

12 MR. SHOWALTER: Yes. I want to just
13 briefly mention an issue about reporting on the
14 partner change. I think we mentioned that
15 yesterday briefly at the end of the day.

16 In my former life, I was actually the
17 partner that approved all partner changes in KPMG.
18 And in here -- so I sort of have a feeling about
19 all the changes that take place. And I know you
20 carved out the one about if you're just at the end
21 of your term, you don't have to report that one.

22 I would suggest you consider one other,

1 and it is if you retire in normal course. You'd be
2 surprised how many times that happens. And so,
3 just trying to think about lessening the burden of
4 reporting would be related to. Obviously, if you
5 are at the end of the 5 years, you don't need to
6 report that. But also some partners get on the
7 account, but because of mandatory retirement age,
8 they don't go to full term.

9 So I would suggest that as a way of
10 reducing that burden. But you'll be surprised how
11 many partner changes take place for very valid
12 reasons.

13 MS. RAND: The proposal isn't requiring
14 disclosure, though, of reasons of why the partner
15 change occurred. You would just indicate the name.

16 So --

17 MR. SHOWALTER: Right.

18 MS. RAND: So I guess I'm -- yes, if you
19 can clarify that?

20 MR. SHOWALTER: But you particularly
21 carved out if you're at the end of the 5-year
22 rotation, you don't have to report that. I thought

1 you carved that out, and you said you didn't have
2 to report that.

3 So I'm suggesting one other one you may
4 want to consider is if you're at the end of your
5 mandatory retirement age, you wouldn't need to
6 report that change either.

7 MS. RAND: No, the change -- no, you just
8 disclose the name.

9 MR. SHOWALTER: Right.

10 MS. RAND: So if there is a change
11 regarding if it's the end of five or four --
12 whoever is the partner signing the report --

13 MR. SHOWALTER: Right. Right.

14 MS. RAND: -- just discloses the name.

15 So it's not --

16 MR. SHOWALTER: I may have
17 misinterpreted. I thought you carved out if they
18 were at the end of the mandatory rotation, you
19 didn't disclose that one.

20 MS. RAND: Disclosure of the name would
21 be required in all cases.

22 MR. SHOWALTER: Okay.

1 MS. RAND: And reasons are not part of
2 the required disclosure.

3 MR. SHOWALTER: Okay. Thank you.

4 MR. BAUMANN: Neri?

5 MR. BUKSPAN: Just an observation. If
6 you do have the partner sign, why do you need to
7 disclose change? It's obvious.

8 MR. BAUMANN: I think it's just saying
9 we're not requiring disclosure of change. We're
10 requiring the identification of the partner who is
11 responsible for that engagement that year.

12 MR. BUKSPAN: Correct. Perfect. Thanks.

13 MR. BAUMANN: That's what we're
14 requiring.

15 MR. BUKSPAN: Yes. All right.

16 MR. BAUMANN: Steve Harris?

17 MR. HARRIS: Do the firms accumulate this
18 threshold information as a matter of course, and to
19 what extent is there any administrative burden or
20 cost associated with it?

21 MR. GALLAGHER: Steve, in terms of hours,
22 you mean? In terms of where the work is done? I

1 think that would be relatively easy. I think the
2 answer is yes. We have it, and it would be to
3 those who have done it, it's pretty easy to
4 accumulate.

5 MR. KOLINS: And after that, I think
6 there's a provision in the release talking about
7 estimates, if you don't have the exact number in
8 hand. So, yes, I kind of agree with Mike. It's
9 probably not significant additional burden. It's
10 in the normal course. It's just one additional
11 thing to get together at the time of the filing.

12 MR. BAUMANN: And that's one of the
13 reasons why we went with that metric is we believe
14 that firms did capture hours in the normal course,
15 and therefore, it wouldn't be a significant burden.

16 Sam? I almost missed you over there,
17 Sam.

18 MR. RANZILLA: I just think there's been
19 talking around each other here on this change in
20 partner. At least the way I understand it is
21 you're not proposing any Form 3 requirement to have
22 a change when a partner changes off an account. I

1 thought it was you're asking the question as to
2 whether or not there ought to be a Form 3
3 requirement?

4 To Neri's point, you'll be able to see
5 that the partner changed from one report to
6 another. The way I understood your proposal was
7 that's all we're proposing, but do we need to do
8 something like a Form 8-K in between? But that's
9 not actually a part of the rule proposal, is it?

10 MR. BAUMANN: Correct.

11 MR. RANZILLA: Okay. I just wanted to
12 make sure I understood.

13 MR. BAUMANN: Joe Carcello?

14 MR. CARCELLO: Real quick, Marty. Have
15 you thought -- or maybe Mike, since he raised the
16 issue of hours. Have you thought about having the
17 disclosure threshold not tied to hours, but tied to
18 valuated hours?

19 So you would take partner billing times
20 hours, manager billing times hours, staff billing
21 times hours, and then use whatever threshold of the
22 valuated number rather than the raw hours. Because

1 what Mike is saying is not all hours are created
2 equal.

3 Have you considered that, or what would
4 Mike's reaction be or other firm people? I'm not
5 sure I like it, but it's a way to --

6 MR. GALLAGHER: I'd be happy to share.
7 My reaction is that I understand why the team went
8 with hours because that is objectively measurable.
9 It's pretty easy to get to, and I'm not sure I've
10 got a better alternative. My only concern was,
11 Joe, just as you articulated, not all hours are
12 created equally. I'm just not sure I have a better
13 one.

14 That could be another way of thinking
15 about it. What I'm concerned about is do you
16 create potentially a misleading picture around if
17 you use just a pure, objective mathematical
18 calculation? And again, until I have a better
19 solution, hours is as good as anything. But we
20 will be looking hard at how do we best express the
21 qualitative and the quantitative in terms of where
22 the work is done if we're going to go in this

1 direction?

2 MS. RAND: Just to -- I just want to
3 point out there is Question 28, since there has
4 been much discussion, on this issue about if hours
5 is the appropriate metric or something else. So
6 Question 28 says should the Board require a
7 discussion of the nature of the work performed by
8 other participants in the audit, in addition to the
9 extent of participation as part of the disclosures?

10 So that would get to, you know, should
11 there be some discussion about, well, they spent a
12 lot of time, but it wasn't on the significant risk
13 areas. So we are asking questions around that
14 because we recognize that could be a consideration.

15 MR. BAUMANN: Barbara?

16 MS. ROPER: Just quickly on that point.
17 I think nature of the work performed strikes me as
18 a much better approach than this hours times pay,
19 or whatever, in part because of one of the reasons
20 you outsource is because you are paying less than
21 hours devoted to doing the same things under
22 different pay scales would look like they weren't

1 equivalent when they are. So that doesn't strike
2 me as a particularly good measurement.

3 But nature of work strikes me as directly
4 relevant to what you want to know with this
5 information is, you know, who's doing the work and
6 how significant is the work that they're doing?

7 MR. BAUMANN: Sam?

8 MR. RANZILLA: I agree with Mike that at
9 least where we are is hours appears to be a fairly
10 reasonable place, although we recognize that no
11 measure is going to be perfect. Trying to gauge
12 the hours on the relevance of the hours I think is
13 going to be extraordinarily difficult.

14 And from my perspective, this is an
15 exercise that will occur in the last 2 weeks of an
16 audit, and the last thing I want the audit partner
17 to be doing is trying to figure out whether it's
18 6.3 percent or 8.1 percent of the hours through
19 some complicated logarithm that the team had to
20 develop. I'd say we keep it simple and get people
21 focused on actually completing the audit, as
22 opposed to it.

1 And maybe there are some ways you can
2 bucket hours so that you give -- so, in other
3 words, 10 to 15 percent gets the same value, and
4 then you don't worry about some of the nuances. So
5 my only suggestion is let's try to keep this thing
6 simple. And if it doesn't work, you've always got
7 the chance to amend it, and we'll find a better
8 way.

9 MR. BAUMANN: That's a good point, Sam.
10 And that was why we came out with hours and the
11 ability to estimate hours reasonably through the
12 end of the period because we didn't want it to
13 interfere with the important aspects of completing
14 the audit. And since this is done in the normal
15 course of events, we thought this would not add
16 significant burden in that regard.

17 Maybe Arnie Hanish, and maybe we can
18 close down this topic?

19 MR. HANISH: That would be great.

20 [Laughter.]

21 MR. BAUMANN: You get the last word,
22 though.

1 MR. HANISH: All right. Well, listening
2 to all this, I support Sam 100 percent. We've got
3 to find a way to keep it simple. I hear what
4 you're trying to accomplish. But in the end, we're
5 the ones who are going to pay for all this extra
6 time that they're going to take to try to figure
7 out if it's 3 percent, 4 percent, 5 percent or what
8 are the measures.

9 The companies are going to pay for this,
10 and let's just, quite frankly, come up with a way
11 to keep it simple and have a threshold at a high
12 enough level that we don't have to deal with small,
13 incremental activities, offshoring, or whatever it
14 might be. But I guess I'd just ask you to, please,
15 keep it simple in the spirit of what you're trying
16 to accomplish.

17 Thank you.

18 MR. BAUMANN: Good. Well, thanks for all
19 of those valuable additional comments for us to
20 think about as we go through this, and we'll look
21 forward, obviously, to the comment letters.