

AN OFFERING FROM THE BDO CENTER FOR CORPORATE GOVERNANCE
AND FINANCIAL REPORTING

BDO FLASH REPORT

CORPORATE GOVERNANCE



SUBJECT

PCAOB REPORT ON INSPECTION OBSERVATIONS RELATED TO AUDITOR COMMUNICATIONS WITH AUDIT COMMITTEES

SUMMARY

The PCAOB issued a [report](#) to provide the public with information regarding audit firms' and audit engagement teams' implementation of, and compliance with, PCAOB Auditing Standard No. 16 (AS 16) [AS 1301¹], *Communications with Audit Committees*, and other PCAOB rules and standards related to audit committee communications. The report is based on the PCAOB's 2014 and preliminary 2015 inspection results related to domestic and non-U.S. registered audit firms. AS 16, which became effective in 2012, requires an effective two-way dialogue in which the auditor is to communicate with the audit committee regarding certain matters related to the conduct of an audit and to obtain certain information from the audit committee relevant to the audit. In addition, there are specific audit committee communication requirements contained in other PCAOB auditing rules and standards that the PCAOB considered which encompass matters relating to independence; risks of material misstatement, including fraud risks; and scope of tax services; among others.²

For the 2014 and 2015 inspection cycles, the PCAOB performed inspection procedures related to compliance with audit committee communications, as well as, specific procedures to evaluate firms' actions to implement AS 16 [AS 1301] in their audits. Procedures performed varied by size of the audit firm being inspected.

According to the report, PCAOB inspectors found that most audit firms inspected in 2014 had incorporated the requirements of AS 16 [AS 1301] into their audit methodologies, introduced relevant practice aids, or provided training to their partners and staff. Preliminary results from 2015 inspections show similar results.

For the 2014 inspection cycle, the PCAOB indicated that instances of noncompliance noted were more often identified in audits conducted by firms other than member firms of the

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¹ In March 2015, the PCAOB adopted amendments to reorganize and renumber its auditing standards effective December 31, 2016. AS 1301 represents the new number assigned to PCAOB AS 16.

² Refer to Appendix B of AS 16 [AS 1301]) for a listing of related PCAOB standards and rules.

largest six global networks. These included a failure to (1) communicate an overview of the overall audit strategy, timing of the audit, and all of the significant risks the firms had identified; (2) communicate, where applicable, that the firm believed there was substantial doubt about the issuer's ability to continue as a going concern and that it expected to include an explanatory paragraph to that effect in its audit report; and (3) sufficiently document oral communications made to the audit committee regarding certain matters related to the conduct of the audit.

The Inspections staff identified some instances where firms had incorporated the requirements of AS 16 [AS 1301] in their audit methodologies, but engagement teams did not use the revised methodologies or practice aids when planning or documenting their audit committee communications.

For the 2015 inspection cycle, preliminary inspection results indicate the number of inspection deficiencies related to audit committee communications required by AS 16[AS 1301] has remained consistent with the 2014 inspection cycle. However, these inspection deficiencies were more frequently identified in triennially inspected firms that were inspected for the first time under this standard.

PCAOB interviews with audit committees generally indicated that effective two-way communication with auditors is occurring. There continues to be an emphasis and focus by regulators, including the PCAOB and SEC, and others related to the profession both domestically and globally on the audit committees' oversight of the external auditor as a key element to ensuring audit quality in capital markets.

BDO encourages both audit committees and auditors to read the PCAOB report, recognizing that the communications between the audit firm and the audit committee is fundamental to reliable and high quality audits. For additional audit committee tools and resources, visit BDO's Corporate Governance page at: <https://www.bdo.com/services/assurance/board-governance/overview>.
