



ICGN

International Corporate Governance Network

J. Gordon Seymour
General Counsel and Secretary
Office of the Secretary
Members of the Public Company Accounting
Oversight Board (PCAOB)
1666 K Street, NW
Washington, D.C. 2006-2803 USA

By email: comments@pcaobus.org

29 February 2012

Dear Mr. Seymour and Board Members

**Re: Consultation input on PCAOB Rulemaking Docket 030
PCAOB Release No. 2011-008, December 20, 2011.
Proposed Auditing Standard Related to Communications with Audit
Committees**

Thank you for the opportunity to comment on the Re-proposed Auditing Standard, *Communications with Audit Committees*, issued by the Public Company Accounting Oversight Board (PCAOB). We are writing on behalf of the International Corporate Governance Network (ICGN). The ICGN is a global membership organisation of institutional and private investors, corporations and advisors from 50 countries. Our investor members are responsible for global assets of U.S. \$18 trillion.

The ICGN's mission is to raise standards of corporate governance worldwide. In doing so, the ICGN encourages cross-border dialogue at conferences and influences corporate governance public policy through ICGN Committees. We promote best practice guidance, encourage leadership development and keep our members informed on emerging issues in corporate governance through publications and the ICGN website. Information about the ICGN, its members, and its activities is available on our website: www.icgn.org.

The purpose of the ICGN Accounting and Auditing Practices Committee (AAPC or the Committee) is to address and comment on accounting and auditing practices from an international investor and shareowner perspective. In doing so, the Committee, through collective comment and engagement, strives to help to ensure the quality and integrity of financial reporting around the world. More information about the Committee can be found via: http://www.icgn.org/policy_committees/accounting-and-auditing-practices-committee/

The ICGN wishes to express our support for the PCAOB's comprehensive and fundamental review of auditor communications with the audit committee and we are pleased to provide general comments as well as comments on some of the specific issues raised in the document. In particular, we are encouraged by the fact that the PCAOB is consulting stakeholders, especially investors, shareowners and the wider investor community, to better understand an auditor's communications with the audit

committee and to seek suggestions for possible improvements to the proposed standard. We would also like to emphasise that investors are primarily interested in - and should be provided with - information regarding all current and foreseeable material issues, rather than a focus on a myriad of details on non-material factors.

We would like to express our continuing commitment to the concept of best practice that contributes to the efficiency and effectiveness of capital markets, including credible, high quality financial reports which serve the needs of investors and other users of financial information. Investors need to have confidence in financial statements in using them to evaluate and make investment decisions, and hold management to account. The integrity and quality of financial reports is supported and strengthened by a robust external independent audit and an active vigilant audit committee.

Clarity of Roles

A key audit committee role is to uphold audit quality and to protect the interests of investors. Robust and open communications between the external auditor and the audit committee supports and promotes this confidence.

The ICGN believes the audit committee of the board has an important role in ensuring the integrity of financial reporting and ensuring quality oversight of financial reporting on behalf of shareowners. Communications that serve to enhance their role are important and helpful to shareowners. The auditor, on the other hand, issues the audit report for the benefit of shareowners and the capital markets, not only for the benefit of the audit committee. It is in the course of undertaking the audit, the auditor may glean information useful to the audit committee as well as to shareowners and future investors.

We also believe it is most important that the specific roles of the auditor, the audit committee and management are clearly outlined within the standard, so there can be no confusion in this respect. No one party should encroach on the legitimate role of the others.

Content

We are particularly interested in any auditor communications and information that may be material to the market price of the company shares. In particular, this could include:

- Key business, operational and audit risks which the auditor believes exist, and which the auditor has considered when conducting the audit;
- The auditor's perspective on what are the key assumptions used in judgments that materially affect the financial statements, and whether those assumptions are at the low, most likely, or high end of the range of possible outcomes;
- The appropriateness of the accounting policies adopted;
- Changes to accounting policies that have a significant impact;
- The methods and judgments made in valuing assets and liabilities;
- Any unusual transactions;
- Accounting applications and practices that are uncommon to the industry;
- Identification of any matters in the Annual Report that the auditors believe are incorrect or inconsistent with the information contained in the financial statements or obtained in the course of their audit;

- Key audit issues and their resolution which the audit partner documents in a final summary audit memo;
- Quality and effectiveness of the governance structure and risk management (including internal controls);
- Evaluation of whether there is a substantial doubt about the company's ability to continue as a going concern for a reasonable period of time; and
- A view on how the entity compares to its peers in the effectiveness of its internal controls and financial reporting practices.

Communication

We would like to see robust communications between the auditor and the audit committee that are not formulaic nor adopt a 'checklist approach'. Further the ICGN would like to avoid a compliance approach to these communications. Minor matters should not be included unless they are indicative of higher level issues and risks. The dialogue should be a two way meaningful exchange on important matters and not clouded by minutiae. However we also believe that a record of the exchange should be kept in order to avoid misunderstandings. Ultimately, the ICGN would like to see a robust, substantive exchange between the parties, aimed at helping to ensure effective communications in promoting transparent and reliable information in the conduct of the audit.

Scope

Whilst it seems that the new standard does not impose any new requirements on auditors, it does helpfully clarify the nature and style of the communications between the auditor and the audit committee. The ICGN is pleased to see references to a number of specific matters, not necessarily placed here in order of importance, which should be discussed with the audit committee, including:

- The audit strategy and structure and timing of the audit;
- Auditor liability;
- The auditor's assessment of risk areas, including fraud risks;
- The auditor's use of external experts and other auditors;
- Difficult and contentious issues that arise in the course of the audit;
- Significant unusual transactions
- Significant accounting policies, judgments and estimates; and
- Going concern evaluation and issues and other matters.

To ensure high quality audits, we also believe audit committees should not agree to limit the liability of outside auditors and ensure this is clearly expressed in its communications with the external auditor and shareowners.

However we would not want the above list to be the only matters considered in the communications envisaged. We believe both the auditor and the audit committee should be free to raise any matter each deems important. This then would lead to the full and frank discussions the investor community is seeking in the relationship. The list should therefore be viewed as a non-exclusive guide to some topics that may be canvassed. We would like to see included in the standard mention of the auditor's view of the quality, clarity and completeness of the financial statements.

A particular focus of the exchange should be any risks faced by the entity, whether they are financial or business risks. Particularly helpful to the work of the audit committee would be the auditor's view of the internal controls of the entity.

The better audit committees may already have these kinds of communications in place. However recent experience in the financial crisis has shown that there is sufficient concern in many entities that audit committees may not be receiving adequate information from management on company financial reporting and the work of the auditor. This is compounded by ineffective communications between the auditor and the audit committee. Therefore we support the standard and its attempt to make these communications more robust, which we see will strengthen the audit committee's oversight function.

To summarize, the areas of specific comment we would wish to bring to your attention are as follows:

- The proposal mentions 'significant unusual transactions'. In order for auditors to discuss these with the members of an audit committee, the ICGN believes that both 'significant' and 'unusual' need to be defined or at the very least clarified.
- The ICGN believes that the communications between the auditor and the audit committee should not be constrained by written reports. However a good and relatively detailed record of the discussions should be kept in order to avoid later misunderstandings.
- Given that the standard is expected to be applicable in the United States (US) and that there are many companies that come under US jurisdiction as well as another jurisdiction, some evaluation of the extraterritorial effects of the standard may be useful.

If you would like to discuss any of these points, please do not hesitate to contact Carl Rosen, our Executive Director, at +44 207 612 7098 or carl.rosen@icgn.org. Thank you for your attention and we look forward to your response on the points above.

Yours sincerely,



Christianna Wood
Chairman of the ICGN Board of Governors



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Co-Chair, ICGN Accounting and
Auditing Practices Committee



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