

LEGAL UPDATES

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# PCAOB Proposes Major Reforms to Auditor Reporting Standards

The Public Company Accounting Oversight Board (PCAOB) has proposed new auditor reporting and other information standards that would significantly increase auditor involvement in the annual report on Form 10-K. The proposal would retain the current “pass/fail” model of the auditor’s report but require the auditor to communicate a wider range of information specific to the particular audit.

The proposed auditor reporting standard, *The Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*, would require the auditor to disclose:

“Critical audit matters” identified during the course of the audit that are included in engagement completion documents, reviewed by the engagement quality reviewer or communicated to the audit committee.

“Critical audit matters” are defined as matters that (i) involved the most difficult, subjective or complex auditor judgments, (ii) posed the most difficulty to the auditor in obtaining sufficient audit evidence or (iii) posed the most difficulty to the auditor in forming an opinion on the financial statements.

Auditors would be required to (i) identify the critical audit matter, (ii) describe the considerations that led the auditor to determine that the matter is a critical audit matter, and (iii) refer to the relevant financial statement accounts and disclosures that relate to the critical accounting matter.

The standards that require the auditor to maintain its independence from the issuer and the year in which the auditor began its tenure with the issuer.

The auditor's responsibilities for evaluation of information in annual reports filed with the Securities and Exchange Commission (SEC) beyond the financial information contained in the financial statements and audit report (required by the proposed other information standard discussed below), and a statement about the results of the auditor's evaluation.

The second proposal, *The Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report*, introduces a completely new obligation that would require the auditor to report on its review of the other information in annual reports filed with the SEC under the Securities Exchange Act of 1934. This includes the selected financial information, management's discussion and analysis, executive compensation, related party transactions, exhibits and other information incorporated by reference in the Form 10-K, including information incorporated by reference to the proxy statement.

The second proposal extends the auditor's obligations beyond simply reading and considering the information contained in these filings, as auditors are currently required to do. Instead, the proposed other information standard would require auditors to evaluate and identify material inconsistencies with the audited financial statements or material misstatements of fact in the information disclosed in other sections of the annual report. As mentioned above, the auditor also would be required to include a discussion of its obligations and findings in the auditor's report.

### **What This Means to You**

According to the PCAOB, "[t]he proposals are meant to improve the current auditor reporting model by requiring the auditor to communicate specific information about each audit based on audit procedures performed." The PCAOB hopes that the new standards will make the auditor's report more informative and increase its relevance and usefulness to investors and other financial statement users.

Public comments on the proposed standards are due by Dec, 11, 2013. The PCAOB members expect that the proposals will result in further roundtables and possible re-proposals before any final standards are adopted.

As drafted, the proposals would have a profound impact on audits, audit reports and the relationships between auditors and the companies they serve. In addition, if adopted, the proposals will certainly increase audit fees. We will keep a close eye on the ongoing development of these new auditor reporting standards.

Read the full proposal [here](#) and the PCAOB Fact Sheet summarizing the proposal [here](#).

### **Contact Information**

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For more information concerning this or other issues affecting securities or corporate governance, please contact your Husch Blackwell attorney or an attorney in our Securities & Corporate Governance practice.