

PCAOB Highlights Issues for Audit Committees

May 14, 2015 | Client Update | 2-minute read

In the first of what is promised to be a series, the PCAOB issued a [communication](#) to audit committees to highlight key areas of recurring concern in PCAOB inspections of large audit firms and emerging risks to audits. This *Audit Committee Dialogue* includes questions that the PCAOB encourages audit committees to ask their auditors.

The biggest issues continue to be the auditing of internal control over financial reporting (ICFR) and assessing and responding to the risks of material misstatement. On ICFR, the PCAOB inspections often found that an auditor did not perform sufficient procedures to test the effectiveness of controls, and where deficiencies were identified, sometimes the auditor did not sufficiently evaluate whether they constituted material weaknesses. Audits of ICFR should identify material weaknesses even before a material misstatement occurs. Questions that an audit committee could be asking include inquiring about an auditor's approach to evaluating the company's ICFR for significant or unusual transactions or events, such as business combinations, divestitures and major litigation claims.

In terms of risk assessment and responses, PCAOB inspections have found that audit plans are not always adjusted to account for changes in transactions or locations, and sometimes rely too much on entity-level controls and fail to provide for adequate procedures at locations or business segments that are significant contributors to the operations.

The PCAOB indicates that it is monitoring several new indicators of emerging risks in their inspection planning, including the increase in M&A activities that have resulted in a range of auditing deficiencies, falling oil prices and undistributed foreign earnings which require an auditor to gather evidence to support management's assertions about indefinite reinvestment.

Audit Committee members and others may [sign up](#) to receive future PCAOB updates and may [contact the PCAOB directly](#).

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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