

Audit Committee *Brief*

Evaluating the External Auditor



"I expect that the auditor evaluation tool will serve to form leading practices for evaluating independent auditors and will lead to more consistency in the marketplace."

Robert J. Kueppers
Managing Partner

Center for Corporate
Governance

Deloitte LLP

As annual reports are published, audit committees often conduct an auditor assessment and begin the process of engaging the external auditor for the next year's audit. This issue of the *Audit Committee Brief* provides additional resources to aid the audit committee in performing this assessment.

The audit committee is directly responsible for selecting, assessing, and compensating the external auditors. There is limited guidance on how to perform an evaluation of the auditor, and needs and preferences vary. As a result, practices range from highly formalized processes with extensive documentation to more informal efforts. Common criteria for evaluating the audit engagement team, individually and as a whole, include technical competence, industry knowledge, communication, cohesiveness, independence and professional skepticism, and support provided to the audit committee.

In addition, the audit committee may consider characteristics of the overall audit firm, such as the adequacy of resources, industry experience, financial stability, audit approach, approach to professional development, technological capabilities, quality of thought leadership, and marketplace eminence. PCAOB inspection reports and peer reviews may also be factored into the evaluation.

Auditor annual evaluation tool

A group of leading governance organizations¹ recently released a tool, [Audit Committee Annual Evaluation of the External Auditor](#), to help audit committees evaluate the external auditors as part of the annual reappointment process.

A [press release](#) on the Center for Audit Quality's website states that "[t]he assessment tool is the first outcome of an ongoing collaboration that will allow the participating organizations to leverage their separate efforts to expand access to useful tools and materials, with the objective of strengthening audit committee performance and transparency."

The tool offers a variety of resources for the audit committee to use in the evaluation process, including sample questions to consider in assessing the lead partner, engagement quality reviewer, and overall audit team. Though not intended to be exhaustive, the questions provide a good starting point for discussion and can be adapted for individual companies as appropriate. The questions are divided into three categories:

- The quality of services and sufficiency of resources provided by the auditor
- Communication and interaction with the auditor
- Auditor independence, objectivity, and professional skepticism

The tool also covers prohibited nonaudit services and relevant PCAOB and SEC requirements regarding communications between the auditor and audit committee.

In addition to performing their own assessment, audit committees often solicit feedback from company personnel to gain insight into the external auditors; the tool includes a sample form for this purpose. The form covers the same general topics as the tool's auditor evaluation for audit committees and allows management to make recommendations for improving audit quality.

NYSE listing requirements related to auditor evaluation

The NYSE listing standards require the audit committee to review a report by the independent auditor describing quality control, results of investigations, and independence. The associated commentary states that when the audit committee has reviewed the report and the auditor's work during the year, it will be better positioned to evaluate the auditor's qualifications, performance, and independence.

The standard also specifies that the "evaluation should include the review and evaluation of the lead partner of the independent auditor," and "should take into account the opinions of management and the company's internal auditors (or other personnel responsible for the internal audit function)."



¹ The following organizations contributed to the tool: [Association of Audit Committee Members](#), [Center for Audit Quality](#), [Corporate Board Member](#), [Independent Directors Council](#), [Mutual Fund Directors Forum](#), [National Association of Corporate Directors](#), and [Tapestry Networks](#).



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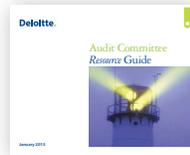
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Click [here](#) or visit the App Store and search for “Deloitte Audit Committee Resources” to download the application.



Additional resources

Several other resources are available to assist the audit committee in its auditor evaluation activities:



Deloitte’s [Audit Committee Resource Guide](#) helps audit committee members and management better understand the requirements, roles, and responsibilities of the audit committee, and includes supporting tools such as a sample charter and a planning tool for the audit committee’s calendar of activities.



The AICPA’s [Audit Committee Toolkit](#)² includes “Evaluating the Independent Auditor: Questions to Consider,” which provides sample questions for the audit committee, chief financial officer, and internal and external auditors.



In August 2012, the PCAOB released [Information for Audit Committees about the PCAOB Inspection Process](#), which is intended to assist audit committees in better understanding the PCAOB’s inspection process and gathering information from auditors about inspections.

In addition, external auditors often have assessment questionnaires for evaluating their performance; Deloitte’s questionnaire is the *Quality Service Assessment Tool*. Audit committees can use such questionnaires, tailor them to fit their needs, or create their own. The assessment can be conducted by having the relevant parties complete the questionnaire in writing or by conducting interviews. Audit committees can also facilitate a discussion about the experiences committee members and others at the company have had in working with the auditors.

Conclusion

Conducting regular auditor assessments helps audit committees effectively monitor audit quality and communicate expectations. Though evaluation practices vary in terms of focus and approach, using resources such as the [Audit Committee Annual Evaluation of the External Auditor](#) and the other materials discussed above can yield valuable feedback that strengthens the relationship between the audit committee and auditors and promotes the continuous improvement of processes.

² Sections of the toolkit are available through Deloitte’s Center for Corporate Governance website by permission. See section 4 on the linked page to access “Evaluating the Independent Auditor: Questions to Consider.”

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