

Corporate & Financial Weekly Digest

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PCAOB Chairman Considers Audit Firm Rotation

In a wide-ranging speech to the SEC and Financial Reporting Institute's 30th Annual Conference on June 2, James Doty, Chairman of the Public Company Accounting Oversight Board (PCAOB) raised for discussion and review the possibility that the PCAOB may require audit firm rotation.

In his speech, Chairman Doty described a lack of "independence and skepticism" that has surfaced over eight years of inspections of the largest audit firms conducted by the PCAOB. He stated that PCAOB inspectors have reviewed more than 2,800 engagements and "discovered and analyzed hundreds of cases involving... audit failures." Mr. Doty attributes such failures to both a lack of professional skepticism and an "inappropriate mindset" that continues to exist despite auditor independence rules. "Auditors are, after all, paid by the clients they are charged with policing. As in other professions, auditors want to advance in their chosen profession which often means keeping the client happy and growing their business."

Given these concerns, Mr. Doty expects that the PCAOB will issue several policy papers in the near term to stimulate discussion as to whether there should be changes to the standard auditors' report, whether the PCAOB can find ways to enhance audit committees' understanding of the PCAOB's inspection process and, finally, whether audit firm rotation should be mandated.

In support of the latter, Mr. Doty stated "...considering the disturbing lack of skepticism we continue to see, and because of the fundamental importance of independence to the performance of quality audit work, the [PCAOB] is prepared to consider all possible methods of addressing the problem of audit quality—including whether mandatory audit firm rotation would help address the inherent conflict created because the auditor is paid by the client."

While Mr. Doty states that he does not have a "pre-determined idea" of whether the PCAOB ultimately should adopt term limits, he states his goal is to "better insulate auditors from client pressure and shift their mindset to protecting the investment public."

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