Questions
for the audit committee
to consider

› Financial reporting
› Internal controls
› Internal auditor
› Independent auditor
Financial reporting

General

• If there was any significant change in the business environment, such as new competition or a change in regulation, how did this change affect judgments and estimates; recoverability of assets, including fixed assets, intangible assets, goodwill and investments; and potential classification issues, such as classification of debt?

• Has there been a voluntary change in accounting principles, such as a change in inventory method from last-in, first-out (LIFO) to first-in, first-out (FIFO)? If so, how did the company decide that this policy was preferable, and will a preferability letter from the auditors be filed with the financial statements? Are there longer-term effects expected from the change?

• Has there been any significant change in accounting estimates during the period? Have there been any significant changes in trends or facts that may indicate estimates should change, such as changes in frequency or cost of warranties, technology changes or an estimated settlement of contingencies? Have there been any changes in the company’s methods for determining significant accounting estimates, or were there significant changes in the nature of the assumptions used during the period?

• Has the company received any SEC comment letters during the period? If so, what was the focus of these letters? Has management made any changes to the financial statements as a result? Are there any unresolved matters?

• Did the company receive a comment letter from the SEC regarding its filings? Were any significant issues raised?

• Were the independent auditors involved in assisting management draft responses? Were their suggestions accepted by management?

• Are there any outstanding comment letter issues?

• Did a restatement of financial statements result from the SEC comment process?

• Did the company have any accounting or financial reporting issues for which it sought pre-clearance of the matter from the SEC?

• Were any new accounting standards adopted during the year? If so, what was the effect on the financial statements? Does the new standard require any new significant judgments or estimates?

• If there was a significant operational issue during the period, such as excessive downtime or rework, how did management consider the following, and what were the results:

  • Contractual disputes and potential effects on accounting, such as revenue recognition and contingent liabilities
  • Appropriateness of inventory valuation, such as whether abnormal costs were expensed
  • Impairment of assets

• Have there been any new or significant changes in contractual agreements that could have an effect on the accounting treatment (e.g., revenue recognition, inventory)? Examples include:

  • Consignment arrangements
  • Bill and hold arrangements
  • Change in shipping terms
  • Product financing

• Have the stringent requirements for bill and hold revenue been met?

• If there was a significant change in the company’s organization during the period, did management consider if financial reporting was affected? Examples include:

  • Discontinued operations
  • Change in segments
  • Exit or disposal obligations, such as contract termination costs or involuntary employee termination benefits under the terms of a one-time benefit
Changes to the company's system of internal controls
Consolidation
Has the company continually evaluated its segment reporting?
As part of management's execution of its business plans, did it consider any financial reporting implications, and if so, what was its conclusion? Examples include:
- Significant property, plant and equipment expenditures, including potential asset valuation issues or contractual issues with vendors
- Business acquisitions
- Were any known errors not recorded? Why were these not recorded? What did management do to assess materiality? Did management consider any control implications for these errors?
- Were any significant deficiencies or material weaknesses identified? If so, how did these arise, and what is the plan to remediate them?
- Have there been any significant subsequent events (i.e., transactions or events that occur after the balance sheet date but before financial statements are issued or are available to be issued)? If so, how have they been recognized in the financial statements (where applicable) or disclosed in the footnotes?
- Has the company disclosed risks and uncertainties that in the near term – within one year from the date of the financial statements – could significantly affect the amounts reported in the financial statements?
- Is the company able to meet obligations as they become due without substantial disposition of assets outside the ordinary course of business, restructuring of debt or equity, or operational improvements, whether these improvements are the result of a change in the company's operating environment or the result of regulatory forbearance?
- Has the company appropriately considered whether conditions or events exist that raise doubts about the company's ability to continue as a going concern?
- Have there been any significant fluctuations in results from year to year, or between actual and budgeted results?
- How do the company's accounting policies compare to leading practices in the industry?
- Does the MD&A adequately explain the company's financial condition and results of operations?
- What recommendations have the independent auditors made relating to the financial reporting process? How has management responded?
- Have there been any disagreements between management and the independent auditors on accounting principles or how to account for a significant transaction?
- Has the independent auditor consulted with its national office on significant issues? If so, what were the issues?

Cash
- Are there any restrictions on the use of cash? If so, are they properly disclosed?
- Is any portion of the cash balance held under formal or informal compensating balance arrangements? If so, are these facts disclosed in the financial statements?
- Is the presentation of the statement of cash flows consistent with previous years? Were there any significant cash transactions where management had difficulty identifying the appropriate classification (e.g., operating versus financing activities) on the statement of cash flows?
- What is the company's policy for including financial instruments within cash equivalents? Does the company appropriately consider Accounting Standards Codification (ASC) 820-10, *Fair Value Measurement*, when valuing such instruments?
- For significant cash in foreign locations, is appropriate disclosure provided?
- For new or unusual items, has the cash flow presentation been fully evaluated?
**Financial instruments**

- How does the company invest excess funds? What are the investment policies on risk and yield?
- Have there been significant changes during the year in the types of investments held?
- Has the company invested in any “exotic” or unusual financial instruments?
- Does the company hold any significant investments in sovereign debt issued by European countries that are experiencing liquidity issues, such as Greece? If so, has the company considered any concentrations of credit risk for disclosure?
- Has the company entered into any interest rate contracts; foreign currency contracts or other types of options, futures, forwards or swap contracts; or any other types of derivatives? How are they disclosed in the financial statements? If so, what is the nature and extent of the use of derivatives? What are the company’s policies and procedures related to entering into these agreements and evaluating them?
- For derivatives, are related gains and losses properly classified, described and disclosed in the financial statements?
- Does the company use derivatives as a hedging instrument and intend for these hedging relationships to qualify for hedge accounting? If so, has the company documented its hedges, and are the periodic assessments of ongoing effectiveness, as required by US GAAP, being performed?
- Has the company considered the counterparty’s credit risk, as well as its own credit risk, when determining fair value of its derivative instruments?
- Does the company have any intercompany loans between entities with different functional currencies for which changes in exchange rates are reported in consolidated other comprehensive income? If so, has the company performed sufficient analysis to determine whether such loans qualify for long-term investment treatment? Independent of the consolidated financial statement treatment, are the foreign currency remeasurement gains and losses on such loans properly recorded through income on any stand-alone financial statements for the borrowing and lending entities?

- How are debt and equity securities classified: held to maturity, trading or available for sale?
- How was fair value determined for financial instruments that did not have a readily determinable market value? If third-party pricing services were used to help establish these values, what has management done to understand how those prices were developed?
- Have “other than temporary” declines in value been considered?
- Are there any liens, pledges or other security interests in financial instruments? If so, are they properly disclosed? Are any contingent liabilities resulting from these transactions appropriately disclosed?
- Has the company issued convertible debt or convertible preferred shares? If so, has the company evaluated whether such a conversion feature requires separate accounting recognition?
- Does the company have freestanding equity derivative instruments – written call options (warrants), written put options, purchased call options, purchased put options, forward share repurchase agreements or forward sale contracts? If so, has the company appropriately considered whether they should be classified in equity or as assets/liabilities?
- When using broker quotes or third-party pricing services to estimate the fair value for different financial instruments, how does the company validate these prices or quotes?

**Accounts receivable/loans**

- How many days’ sales are included in receivables at year-end? How does this number compare to the prior year?
- Are any significant or unusual amounts due from related parties, including officers and employees? How do these amounts compare to the prior year?
- What is the amount of bad debt expense this year? How does it compare to the prior year?
Questions

Financial reporting

How was the allowance for doubtful accounts/loan loss reserves determined? Has there been a change in the methodology or assumptions used in determining the allowance for doubtful accounts/loan loss reserves? If so, why? How was its adequacy evaluated? Has the allowance changed from the prior year in proportion to changes in receivables/loans? If not, why not?

Is there a high concentration of credit risk (e.g., industry, geographic area, sole debtor)?

Are there any significant receivables from European governments experiencing liquidity issues? Has the aging of these receivables deteriorated during the year? Are there any plans to accept bonds or other long-term obligations of these governments in satisfaction of the receivables?

What were the largest accounts or loans charged off this year? Were they reserved at the prior year-end? If not, why not?

Does the company participate in loans or syndications originated by others? If so, what type of independent credit analysis is performed?

Has there been an increase in identified troubled debt restructurings? What types of modifications, concessions or other arrangements is the company providing to its customers? What factors are considered by the company when determining whether to provide customers with payment delays?

Inventories

What accounting method is used to value inventory (e.g., FIFO, LIFO)? Does the company use standard costing? Were all variances analyzed and properly adjusted? When and where were physical inventories taken? Was the book to physical inventory adjustment significant? If so, why? How does the amount of the adjustment compare to the amount at the last physical inventory date?

What procedures were performed with respect to off-site inventories?

What cutoff procedures are in place for accounting for the shipping and receiving of inventories at period-end?

What procedures were performed to make sure that inventory was not overstated by including obsolete or excess stock? What steps were taken to identify obsolete and excess inventory that require provision? How was the provision for obsolete and excess inventory evaluated for adequacy? Were there any significant write-downs?

Was an evaluation performed to determine that inventory is properly recorded at the lower of cost or market?

Are materials and supplies inventories appropriately accounted for? Should significant items that will not be sold be considered for reclassification?

Investments in affiliated entities

Does the company have any subsidiaries accounted for by the equity method? If so, why is this method used, as opposed to consolidation, and is it appropriate?

Has the company appropriately accounted for any investments in partnerships, joint ventures or other affiliated entities?

Are there any variable interest entities (VIEs) that require consolidation by the company? Have the company’s relationships with VIEs been properly disclosed, even if a VIE is not consolidated?

Were financial statement reviews performed for entities in which the company is invested? What procedures were performed to substantiate the valuation of the investments?

Have all intercompany transactions been eliminated in consolidation, as appropriate?

Property, plant and equipment

Are the estimated useful lives and methods of depreciation reasonable for property, plant and equipment? Have any of the estimated useful lives or methods changed from the prior year?

Were there any significant new leases during the period? Did any require treatment as capital leases?


- How does the company account for leasehold improvements? How does it identify the appropriate period over which to amortize the costs of leasehold improvements?
- Did management capitalize any costs associated with material projects during the year? If so, what was the nature of such costs?
- Were there any indicators of impairment during the period? If so, how were these potential impairments evaluated, and what were the results? For example, did the indicated value only slightly exceed the carrying amount of the asset?
- Did management assess current-year activity (e.g., purchases of property, plant and equipment; entering into new leases; changes in laws, regulations or contracts) for any new asset retirement obligations? Did management assess for significant changes in estimates, such as for expected amounts or timing, for existing asset retirement obligations?
- Have any assets remained as in process for an extended period?
- What analysis did management perform to determine whether any assets should be classified as held for sale? If assets are classified for sale, were impairment and discontinued operations classification considered? If so, what was management’s conclusion?

Other assets

- What is included in other assets? Is the classification as short or longer term appropriate?
- As with property, plant and equipment, were there any indicators of intangible asset impairment? If so, how were they evaluated, and what were the results?
- Are the carrying amounts of goodwill reviewed at least annually to determine whether there has been an impairment in value? How are these carrying amounts evaluated? Are there any deferred charges? If so, have they been evaluated for recoverability?

Current and non-current liabilities

- What procedures were performed to determine that there are no significant unrecorded liabilities?
- Are there any significant, unusual accruals? What significant year-end accruals have been recorded as part of the close process?
- Has the company modified, converted or extinguished outstanding debt during the year? If so, how did the company determine whether the transaction should be considered a modification or extinguishment of the original debt instrument for accounting purposes? Has the company considered whether the transaction would qualify as a troubled debt restructuring?
- Is the company in compliance with the provisions of its loan and debt agreements? Is the company in danger of not complying with such agreements during the next year?
- Has the company considered the proper classification of debt as current or non-current, particularly when considering covenant violations, covenant waivers and grace periods?
- What assets are pledged to secure borrowings? Have pledged assets been disclosed appropriately in the financial statements?
- Has the company issued guarantees of the debt of others? If so, are these guarantees properly disclosed in the financial statements?
- Have the company considered the necessity for, or adequacy of, environmental remediation liabilities?
- Are the assumptions used to value the pension benefit and other post-employment benefit obligations reasonable? Were there any changes in the assumptions this year as compared to last year? Were there any plan amendments during the last year?
- Have guarantor financial disclosures been properly considered?
Contingencies

- Were any significant issues raised by legal counsel about litigation, contingencies, claims or assessments? If so, how have these matters been reflected in the financial statements or footnote disclosures?
- Were any commitments or loss contingencies indicating the potential incurrence of a liability or the possible impairment of an asset not provided for or disclosed in the financial statements? If these matters were not recognized or disclosed because the probable or reasonably possible losses could not be estimated, did the company disclose that such an estimate could not be made?
- What is the company’s process for determining whether a range of loss can be reasonably estimated? Does the company reassess whether a range of loss can be reasonably estimated each reporting period?
- Have disclosures related to loss contingencies evolved over time to include more quantitative information as the loss contingency progresses?
- Where applicable, has the company disclosed the amount of exposure above the accrued amount that is reasonably possible of occurring (i.e., where the estimated loss is a range and the company has accrued the low point on the range)?
- Did management identify any other contingencies that require accrual or disclosure, such as product recalls or environmental obligations?
- Were the legal letters requested by the independent auditor received from all appropriate attorneys?

Shareholders’ equity

- Are any of the company’s equity instruments mandatorily redeemable or redeemable at the option of the holder? If so, has the company evaluated whether those instruments should be classified outside of permanent equity?
- Does the company have any non-controlling interest that is redeemable outside of the company’s control? If so, has the company evaluated whether those interests should be classified outside of permanent equity?
- Are there any restrictions on the use of the retained earnings of either the parent or its subsidiaries?
- Are there any restrictions due to the issuance of preferred stock or on the purchase or use of treasury stock?
- Does the company’s state of incorporation allow for treasury stock presentation, or is repurchased stock deemed retired?

Revenue and expenses

- How does the company’s revenue recognition policy compare with those of other companies in the same industry? Has the company’s policy changed in the current year? Has the company entered into new lines of business or product sales that require it to reconsider its existing revenue recognition policies?
- Has the company properly disclosed its policies relating to different classes of revenue transactions?
- What are the company’s terms of sale and warranty policies? Have they changed from the prior year? If so, how?
- Has the gross profit percentage changed significantly from the prior year or during the year? If so, why?
- Are any unusual or nonrecurring items of revenue or expense included in the financial statements?
- What analyses have management and the auditors performed to consider whether complex revenue recognition issues, such as multiple element arrangements, exist and how to properly account for them?
- Do any industry-specific accounting principles apply to the company? If so, how do they differ from the general revenue recognition principles?
- How has management considered how the company may be affected by the proposed new revenue recognition guidance?
- How does the company account for rent expense relating to operating leases, including leases with option periods and escalating rent?
- Have website development costs been appropriately accounted for?
- How have loss contingencies been accounted for? How have they been disclosed?
• Has the company properly accounted for stock-based compensation? What are the significant assumptions used by management to estimate the fair value of stock options granted?
• Has the company modified any share-based payment arrangements during the year? If so, how do those modifications affect the compensation cost recorded on the financial statements?
• Has the company entered into any new employment contracts with key executives? If so, how has the company accounted for changes to executive compensation arrangements?
• Have the company’s earnings-per-share calculations given effect to recent capital transactions or employment contracts that may involve dilutive securities?

Income taxes

• Is there an unusual relationship between income before taxes and income tax expense? If so, what caused the unusual relationship, and have significant reconciling items been disclosed?
• What is the effective tax rate this year, and how does it compare to the prior-year rate?
• Does the company have significant earnings in foreign jurisdictions with low tax rates? If so, has the company disclosed the effect of such earnings on the effective tax rate?
• Has the company asserted that foreign earnings are indefinitely reinvested? If so, has the company considered the effect that such an assertion could have on liquidity (e.g., where the majority of cash is held by foreign subsidiaries and repatriation would result in significant income tax implications)?
• Have there been any changes in tax laws, rates or methods? If so, how have they been recognized in the financial statements?
• Has the company recorded a liability for uncertain income tax positions based on the recognition and measurement criteria described in ASC 740-10 (formerly FIN 48)?
• What is the company’s process for identifying uncertain tax positions? How does the company evaluate and continually reassess the likelihood that these positions will be sustained by the taxing authority?

Related parties

• Are there significant transactions with related parties? What was done to determine that they are appropriate, properly accounted for and adequately disclosed in the financial statements?
• If other auditors have been involved in the audit of the financial statements, what communication has taken place to determine that all significant transactions with related parties are identified?
• Are the disclosures in the financial statements regarding related parties complete and accurate?

Structured transactions (including those involving special-purpose entities)

• What is the business purpose of the structured transaction?
• Can the structured transaction be understood and explained by management?
• What were the accounting implications of the transaction?
• Does the disclosure of the structured transaction include information critical to investors’ understanding of the transaction’s business purpose and economics?
Internal controls

General
- What are management’s processes and criteria for evaluating identified deficiencies for significance, including significant deficiencies and material weaknesses?
- Is the segregation of duties adequate? Is it prohibited for one person to both initiate and approve transactions? If not, what steps are taken to enhance the segregation of duties?
- Has the company performed a fraud risk assessment? What fraud risks were identified as a result of the assessment? What are the company’s antifraud programs and controls to mitigate the identified fraud risks?
- Does the company have a formal code of conduct?
- Are there adequate controls over the approval and monitoring of special transactions, such as related-party transactions, securitizations using special-purpose entities and other structured transactions?
- How is the company using the internet for e-commerce and communications? Has management assessed the adequacy of controls related to this technology, including the security, privacy, confidentiality and reliability of information, as well as the systems supporting it?
- Does the company have an appropriate business continuity plan, and if so, has that plan been tested recently?
- Are review-level controls sufficiently precise to identify errors of importance?
- How does the company evaluate and test controls over electronic evidence (including spreadsheets)?

Scope
- Are the company’s resources sufficient to adequately assess internal control over financial reporting this year?
- How will the audit of internal control over financial reporting be coordinated with management and the internal auditor?
- What factors will be considered to determine how much the tests of controls performed by others will be used?
- Have specific areas been identified where the independent auditor intends to use the work of management and internal audit as part of the audit of internal control?
- How will the locations to visit for the audit of internal control over financial reporting be selected, and how does that selection process differ from the audit of financial statements?
- What percentage of total assets, revenue and pretax income will be obtained from the locations selected for testing in the audit of internal control over financial reporting?
- Will any operations be excluded from the internal control assessment?
- How will control deficiencies and planned corrective actions be tracked, evaluated and communicated to the audit committee?
- How will IT-dependent controls be assessed for effectiveness?
- What is the scope of IT general controls that will be included in the audit of internal control over financial reporting?
- How will the independent auditor’s assessment consider and evaluate controls over critical accounting estimates and judgmental areas?
- What specialists will be involved in evaluating controls over complex, judgmental and IT-dependent processes?
- How will the controls over accounting systems that have been outsourced to a third party be tested?
- What are the most important changes to internal control the company needs to make in the future?
- How does the company ensure that all electronic audit evidence has been identified and how do they evaluate and test the governing controls for electronic audit evidence, including spreadsheets?
- Have there been any significant changes to the IT environment – system implementations, implementation of other emerging technologies (e.g., cloud). If so, how will the implementation and continuing environment be assessed for effectiveness?
• How do you understand and document the flow of business processes (i.e., flowcharts) to ensure that the appropriate identification of risks and controls (application, IT-dependent and manual) have been designed and implemented to address them?
• Does the company employ a continuous control monitoring technology (i.e., governance, risk and compliance), and if so, how would it be assessed for effectiveness?
• Does the company have an internal or external footprint in emerging technologies, such as the cloud or mobile computing, and if so, how would it be assessed for effectiveness?
• How many applications are in scope? What processes are supported by outsourced applications?
• How are we leveraging technology to identify, document and test controls?
• What changes to the IT environment are expected over the next 12 to 24 months? What is the expected impact on controls as a result of the planned changes?
• If applicable, is the company prepared to be compliant with the new COSO internal controls framework by December 15, 2014? (Companies who choose to stay on the old framework must publicly disclose they are doing so.)

Reporting matters
• What significant deficiencies and material weaknesses in the company’s internal control over financial reporting were identified?
• For material weaknesses identified, what are the underlying causes of the weaknesses? For example, are they systemic or confined to a particular area?
• How did management respond to identified significant deficiencies and material weaknesses?
• Did management implement new controls or strengthen existing procedures to correct material weaknesses or significant deficiencies before year-end? If so, did management consider whether the reason for the change and surrounding circumstances represented material information that should be disclosed?
• Did management exclude any recently acquired business or other consolidated entities from its assessment of internal control over financial reporting?
• Does management plan to improve its internal control assessment process in the future?
• What form of opinion does the independent auditor expect to issue for the audit of internal control over financial reporting?
• If applicable, is the independent auditor satisfied with management’s proposed language in its report on internal control over financial reporting to disclose material weaknesses that exist as of year-end? Do management’s disclosures appropriately describe the circumstances relating to the material weakness and management’s plans to remediate?
• How will any identified significant deficiencies and material weaknesses affect the independent auditor’s strategy regarding the audit of the financial statements?
• Did the independent auditor have any disagreements with management over the characterizations of control deficiencies?
• What are the independent auditor’s observations about the effectiveness of the company’s control environment, including the tone at the top?
• Did the independent auditor identify any control deficiencies that could increase the risk of misstatements due to fraud?
• Did the internal auditor’s or independent auditor’s audit procedures uncover any instances of employee fraud, questionable or illegal payments, or violations of laws or regulations?
Internal auditor

- Does the internal audit department evaluate its charter regularly to confirm that it is still appropriate? Does the charter specify that the internal audit responsibilities are limited to roles that will not hinder objectivity?
- Are the department’s size and structure adequate to meet its objectives? Does the department have sufficient resources to accomplish the responsibilities outlined in the charter?
- What role will internal audit play in management’s assessment of internal control over financial reporting? Has this been defined in the internal audit department’s charter?
- If internal audit is assisting management with its SOX Section 404 assessment, how will this affect the internal audit department’s project plan and resources in other important areas?
- Does the department appear to be objective? What procedures are performed to determine objectivity?
- What is the functional reporting of the department?
- Does the internal audit director have direct access, and report regularly, to the audit committee? Does the audit committee oversee employment decisions relating to the internal audit director?
- Is the experience level of the internal auditors adequate?
- Is the technical knowledge of the department members sufficient for them to perform their duties appropriately? Does the department have an appropriate continuing education program?
- Does the department have members with sufficient information systems auditing experience to address the level of technology used by the company?
- Do internal audit procedures encompass operational as well as financial areas?
- What criteria does internal audit use to establish and prioritize the annual and long-range internal audit plan? What is the current-year plan? Has internal audit coordinated this plan with the independent auditor? Is the department’s work concentrated in areas of high risk, judgment and sensitivity?
- How has the department reacted to changes in the company’s business environment?
- How has internal audit considered the company’s critical accounting policies in its plan?
- How has internal audit considered the company’s most significant accounting estimates and judgments in its plan?
- What types of reports does the internal audit department issue and to whom?
- Does internal audit issue its reports on a timely basis? Do these reports include sufficient detail for effective action by management and the audit committee?
- Has the department made any significant recommendations to management about improving internal controls? Does management have an appropriate and timely response to significant recommendations and comments made by the internal auditors? What follow-up and monitoring procedures are performed by internal audit?
- Was the department’s involvement in the annual audit effective? What could be done in the future to maximize its effectiveness and efficiency? To what extent is outsourcing used in the internal audit function, and what areas are outsourced?
- Does the function have a periodic peer review performed, and if so, what were the results of the latest review?
- How do the internal auditors view the quality of the company’s control environment, including the tone at the top?
- How do the internal auditors view the effectiveness of the company’s antifraud programs and controls?
- Are the internal auditors aware of any known or suspected instances of employee fraud, questionable or illegal payments, or violations of laws and regulations?
- How involved is internal audit in investigating matters raised by whistle-blowers?
- How have the internal auditors assessed the risk of material misstatement, including the risk of material misstatement due to fraud, and what procedures have they performed to respond to those risks?
- Does internal audit advise the audit committee on its assessment of risk and risk mitigation strategies?
Independent auditor

Questions about the firm
- Is your firm independent with respect to the company?
- What are your firm’s independence policies and related processes for monitoring compliance with those policies?
- What are your firm’s quality control policies? What are the results of the latest peer and internal quality reviews? Is the firm the subject of any significant litigation or disciplinary actions by the SEC, the PCAOB or others? Is the firm the subject of any inquiry or investigation by regulatory bodies or others?
- What is your firm’s industry expertise, and does the firm have auditors who specialize in our industry?
- What are your firm’s international capabilities? How will you coordinate communications and audit procedures among international and US offices?
- Is your audit methodology consistent globally?
- Who will be assigned to the audit, and what are their qualifications and industry expertise?
- How much will the engagement partner(s) participate in the audit? Does the lead audit partner have sufficient time?
- Does the partner in charge of this account have the leadership skills and experience to bring all appropriate firm resources to the company when needed?
- How extensive are the firm’s national office and other technical resources? Will the company’s audit team receive prompt and responsive consultations from the national office’s technical partners?
- Does the firm have effective plans for audit partner rotation?
- What are the estimated fees, how are they determined and how will you handle differences between the actual and estimated fees?
- How will the firm use the work performed for the audit of internal control over financial reporting when determining the work needed for the audit of the financial statements?
- How does the firm use technology in its audit?
- How does the firm share knowledge internally?
- If the engagement team cannot resolve an accounting or auditing matter, what other means are available for resolving the issue?

Audit approach
- What is your audit approach?
- How will the internal and external audit functions coordinate their audit procedures effectively?
- What do you consider to be our high-risk areas relating to the financial statements?
- What procedures do you plan in these high-risk areas? How has management assessed the risk of material misstatement?
- What are your procedures for reviewing compliance with the company’s conflict-of-interest policy and code of conduct?
- What are your plans for reviewing officers’ expense accounts and other executive perks?
- What procedures will you perform to address the risk of material misstatement due to fraud, including the risk of management overriding controls?

Multilocation considerations
- How do you determine which company locations to visit for the audit of the financial statements, and what are their assigned scopes? Do you believe any of our business lines are riskier than others? Why?
- Are there locations or areas that you considered high risk in prior years but no longer consider high risk? If so, why has your evaluation changed? What other significant changes from last year have you made in your planned procedures?
- Do you have plans for members of the corporate headquarters audit team to visit key locations? If not, why?
- Are other auditors involved in our integrated audit? If so, do you participate in their scope-setting process? How do you determine whether their work is adequate?
- How do you determine which locations to visit for the audit of internal control over financial reporting, and how does that differ from the selection process for the audit of financial statements?
• What type of coverage (e.g., percent of total assets, revenue, pretax income) do you obtain from the locations that you select for testing, both in the audit of financial statements and in the audit of internal control over financial reporting?

• How are statutory audits integrated into the group audit?

Costs and staffing

• What are your fees for this year’s audit? What caused the change from the prior year? Was the change due to revised audit scope, rate increases or changes in the company’s operations?

• What process does the engagement team have in place to confirm that all services are preapproved, including specific preapproval for internal control-related services?

• Are the audit fees adequate in light of the size and complexity of the company’s business and the risks facing the company and its industry? Has management pressured you to reduce fees?

• What are the engagement team’s qualifications? Have there been any significant changes to the team’s composition?

• What is your plan for audit partner rotation, as required by SEC independence rules? What steps will you take to contribute to a smooth transition to the new partner?

• Has the team experienced significant turnover? If so, what actions are being taken?

• Are you using offshore talent or delivery center resources? If so, how much?

Matters for consideration regarding audit results

Independent auditors are required to present the audit results to the audit committee. The questions below can help guide discussion of the year-end review with the independent auditors:

• What are the company’s critical accounting policies? In other words, what are the policies that are most important to the portrayal of the company’s financial condition and results, and that require management’s most difficult, subjective or complex judgments, often because of the need to make estimates?

• Did management select any material alternative accounting treatments? If so, why did it select them, and do they differ from the accounting treatment preferred by you?

• What are the most significant accounting estimates and judgments? What process does management follow in making those estimates and judgments? Has management changed any significant assumptions underlying these estimates and judgments in the current year? Does management appear to have any bias in its approach to making significant estimates?

• Did you discuss any issues with the SEC or other regulators?

• Did you make any changes in your scope or in planned procedures because of changes in your risk assessments? If so, why did they occur?

• Could any lawsuits or other contingencies significantly affect the company’s financial position? What did the attorneys report to you about the status of litigation or other contingencies? Are the disclosures in the financial statements relating to contingencies adequate?

• Does the company have any significant tax exposure items? What years are open to review by the tax authorities? Has the IRS requested access to your tax accrual working papers for the company? Has the company provided you access to all documentation supporting its tax positions, including third-party tax opinions? Is the company’s accounting and related documentation for tax exposure items reasonable?

• Did you use specialists or consult with your firm’s experts on any significant issues?

• Did you become aware of any known or suspected instances of employee fraud, questionable or illegal payments or violations of laws or regulations?

• Have you identified any deficiencies in management’s anti-fraud programs and controls?

• Are you aware of any other risks and uncertainties that the audit committee should know about?

Changes from prior year(s)

• What is your overall evaluation of the degree of comparability between the presentation of this year’s financial statements and that of prior years’ financial statements? What were the causes of any significant differences in the company’s approach to financial statement presentation? What reclassifications, if any, were made to prior years’ reported amounts?
• Did the company make any initial adoption or modification of an accounting principle where an acceptable alternative accounting treatment would yield significantly different results?
• Did the company make any changes in accounting policies that had a significant effect on the financial statements of the current year or are expected to have an effect on future years? Are any accounting policy changes pending? Was the company’s application of existing accounting policies consistent with that of prior years?
• How do the company’s accounting policies compare with those of other companies in the industry?
• Did the company make any significant changes to internal control over financial reporting during the year, such as changes to implement new systems or to correct material weaknesses or significant deficiencies?

Findings and conclusions
• Do you expect to issue unqualified opinions on the financial statements and internal control over financial reporting? Did you consider issuing anything other than unqualified opinions? How were any concerns resolved?
• Did you note any significant unusual transactions? Are you satisfied with the accounting treatment?
• Did management impose any limitations on the scope of the audit? Were you allowed access to all employees, records and company locations?
• What were the audit findings in the high-risk areas? Do you have any specific recommendations or comments in these areas?
• Did you propose any financial statement adjustments (including changes to disclosures) that management elected not to record? If so, what was management’s underlying reason for not recording the audit differences (e.g., they were immaterial to overall operations), and are you satisfied that the unrecorded differences do not materially affect the financial statements?
• How do you evaluate the significance of these matters when concluding on whether they were material to the financial statements? Have you considered under what circumstances items not determined to be material in the current period could become material in a future period?
• What are your views on the overall quality of earnings reported in light of management’s accounting policies and practices?
• What are your observations regarding the effectiveness of the company’s control environment, including the tone at the top?
• Did management exclude any recently acquired business or other consolidated entity from the assessment of internal control over financial reporting?
• How do the quality and thoroughness of management’s assessment process compare to that of other companies reporting on internal control?
• Were any significant deficiencies or material weaknesses in the company’s internal control over financial reporting identified during the audit?
• What are the underlying causes of any identified material weakness? Are they systemic or confined to one area?
• How did management respond to identified significant deficiencies and material weaknesses?
• Did the audit or internal control identify a significant number of deficiencies? If so, how were these evaluated in the aggregate?
• Did management implement new controls or strengthen existing procedures to correct material weaknesses or significant deficiencies before year-end?
• Are you satisfied with management’s proposed language in its report on internal control over financial reporting to disclose material weaknesses that exist as of year-end? Do management’s disclosures appropriately describe the circumstances relating to the material weaknesses and management’s plans to remediate them?
• Does financial management have adequate resources, such as experienced personnel and the necessary technology?