

# Audit Committee Leadership Network

April 2023

ACLN

VIEWPOINTS

## The relationship between the audit committee and the external auditor

An effective working relationship with the external auditor is vital to an audit committee's oversight of financial reporting. On March 1, 2023, Tapestry Networks convened members of the Audit Committee Leadership Network (ACLN) to discuss good practices used by audit committees when interacting with their external auditors. Members generally described their working relationship with the external auditor as excellent or very good, but they continue to look for ways to further enhance communication and processes.

Members were joined by EY leaders Julie Boland, Americas Area Managing Partner and US Chair and Managing Partner; Linda Hill, Global Client Service Partner; John King, Americas Vice Chair—Assurance; Patrick Niemann, Americas Audit Committee Forum Leader; and Norm Prestage, Global Client Service Partner, to provide insights from the external auditor's perspective.

This *ViewPoints* highlights the following good practices identified as key for working effectively with the external auditor:<sup>1</sup>

- **Cultivate trust and open communication**
- **Use assessments of the external auditor to enhance the relationship**
- **Consider the external auditor's role in ESG reporting**

For a list of meeting participants, see [Appendix 1 \(page 7\)](#); for a list of reflection questions for audit committees, see [Appendix 2 \(page 9\)](#).

### Cultivate trust and open communication

*“Audit firms are our eyes and ears,” one audit chair said. “They have knowledge, skills, and access to people and information at the company that the audit committee doesn’t have. We have to create safe spaces for the external auditor to be able to discuss issues openly and truthfully with the audit chair. How to create that environment is up to each audit chair, but it is immensely important to building a strong relationship.”* Although each relationship is different, members agreed on several good practices:

- **Balance an effective relationship with auditor independence.** While members firmly believe that building effective working relationships with the external auditor is fundamental, they described the need to carefully balance trust and auditor independence.

*“It is undoubtedly good practice to nurture the relationship with external auditors, but it is also important to balance collaboration with maintaining independence,”* one said.

- **Foster open and candid dialogue ...** Two-way, open communication between the audit chair and the engagement partner is critical. A member said that the external auditor should *“feel comfortable raising potential issues quickly and not waiting until it becomes a problem. Sometimes there is a reluctance to bring up a potential issue because it may or may not develop into a situation. But from the perspective of the audit committee, raising any potential issues with the right context and giving the committee an opportunity to ask questions as needed is good practice.”* Another added, *“I want the auditor to share their point of view on things. They can say, ‘I could be wrong, but this is something I’m worried about.’ Make it safe for them to tell you what they are thinking on nontechnical matters.”* Culture and talent concerns can be early indicators of possible issues within a company, yet can be difficult for audit committees to assess on their own. Candid views from the external auditor are often valuable.
- **... through both formal and informal channels.** While the type and cadence of interaction varies, most members have both formal and informal touch points with their external auditors. Typically, they meet one-on-one with the lead engagement partner ahead of the audit committee meeting so that there are *“no awkward surprises for either the audit committee or the external auditor.”* One member noted that a one-on-one session *“helps me understand the issues that need to be raised, which helps me plan the meeting better.”* EY audit partner Norm Prestage described a good practice that he has observed: *“In our premeeting, an audit chair asks me if I have any questions or feedback about management’s slides in the deck. He also presses me on other matters that may not be included in the deck to help identify any other things he should be thinking about.”* Members also recommended regular and less formal *“pulse checks.”* One said, *“I meet with the audit partner once a year over dinner to talk about the relationship and all kinds of issues. We have regular calls. I talk to them before each audit committee meeting. It is a fluid, professional, yet friendly relationship.”*
- **Establish relationships with others on the audit team ...** While most audit chairs regularly interact with the lead audit partner, members said that engaging with all levels of the audit team can add value for both the audit committee and the audit firm. Audit chairs described ways they do this. One said, *“As part of an audit planning meeting, we bring in both the internal and external audit teams. It’s a chance to say thank you, and it is really effective at making the entire team understand how much we, as an audit committee, rely on them and value their insights and views.”* EY’s Julie Boland emphasized the beneficial effect this has: *“Do not underestimate the importance to our teams of the audit chair taking time to meet and speak with them. It’s like gold ... You create a culture that our teams want to be a part of, and it helps attract our best people.”*

- **... and with senior leaders at the audit firm.** Since the audit committee typically works with an external firm beyond any individual audit partner's tenure, members stressed that developing relationships with audit firm leaders more generally is imperative, especially for companies of the size and scale of those represented by ACLN members. One advised, *"Audit chairs have to know the leadership of the firm in addition to the engagement team—any single path of dependency is not good. There has to be an expectation that the leadership will show up with some frequency. I think it helps the relationship enormously."*

### Preparing for partner rotations

Since lead engagement partners play a central role in the relationship between an audit committee and audit firm, members underscored the importance of a smooth partner rotation process, required every five years in the United States. They discussed several good practices:

- **Begin planning early.** Robust planning is essential, and members agreed that the process should start early. *"I begin thinking about rotation in year two of the partner's five-year term,"* one noted. Another described asking the external auditor for *"succession plans on the lead partner, relationship partner, country lead partners—all of the key people—just like we do for management."*
- **Establish clear criteria.** Some audit chairs establish explicit criteria for selecting audit partners, considering factors such as experience, industry expertise, global nature of previous assignments, diversity, and availability for overlap with the outgoing partner.
- **Request multiple options.** Audit chairs should feel comfortable requesting more than one candidate, members said. *"You need to make it clear that you want more than one viable option so that you really do have a choice,"* one said. Another described receiving three résumés but sending them all back and asking for three more because the original three *"did not meet our criteria."*
- **Gather insights from others.** Some members look for references on potential engagement partners, primarily from the audit firm's leadership. *"During the partner rotation process, I reach out to the CEO or other leaders of the audit firm and ask, 'Is this the right partner for my audit? What do you know about this candidate?' We think this is such an important step that we disclose in our proxy that it is part of our process when selecting a new audit partner,"* one said.

## Use assessments of the external auditor to enhance the relationship

Evaluations of the external auditor are an important way for audit committees to assess the overall effectiveness of the relationship. While having an open line of communication between the audit committee and external auditor allows for real-time feedback and course corrections as needed, having an evaluation process is also considered a good governance practice. While most members agreed on this point, the process and cadence of evaluations varied significantly. Some boards conduct formal, written, annual evaluations whereas others use less formal or frequent processes—for example, verbally or on a two-year basis. A few audit chairs found limited value in evaluations, with one saying, *“I have not found a useful auditor evaluation process from the committee’s point of view.”* Members described different approaches and considerations:

- **Seek management’s assistance with the process.** Many members query management for their views on the working relationship with the external audit team and for assistance with creating the process and template for evaluation. EY audit partner Linda Hill noted that in cases where the audit committee or management do not set up an evaluation process, she has initiated an audit firm–led evaluation, but she encourages a *“co-development”* process to ensure a comprehensive assessment rather than selective feedback. Mr. Prestage agreed, adding that if audit firms lead the process, *“there is a risk that the questions will be ones the audit firm is most comfortable answering.”*
- **Don’t stop with management: look to the broader organization for relevant information and feedback.** A member emphasized that it was *“important to hear from all of those within your company dealing directly with the global audit team members. Regardless of whether the feedback is good or bad, insights from all involved with the broader engagement team are valuable to the overall assessment of the external auditor.”* Another said that their process included *“a very formal management-led assessment with 100 finance people around the world to gauge their level of satisfaction with the external auditor. There are discussions about risk exposures, and any occurrences where continuance of the auditor may be questionable. This is all used as input into the audit committee’s discussions on the services we received from the external auditor and their continuation to serve us.”*
- **Identify key areas to evaluate.** Members agreed that clarity and timeliness of the external auditor’s communications, its Public Company Accounting Oversight Board inspection reports, its industry expertise and global presence, and its value add are all important areas to assess. Further, evaluations should extend beyond the lead partner *“and include others involved in the audit, such as the review and second partners,”* one member said.

## Consider the external auditor's role in ESG reporting

Because reporting for environmental, social, and governance (ESG) issues looms large on the horizon (see [ACLN ViewPoints: \*Top concerns for audit committees\*](#)), audit chairs discussed ESG assurance and reporting:

- **Even while regulations are still under development, audit chairs value auditor advice on processes.** While acknowledging that requirements remain uncertain, members described the time and resources they are putting into ESG reporting. One said, *“There is so much work happening within companies around ESG, and it is hard to tell if it is efficient or needed. We asked the external auditor for some guidance on whether all this work is necessary. If it is, is it being done in the way it should be? Is all we’re doing going to yield the results we are thinking it will when the regulations come out?”*
- **Once regulatory requirements are clear, audit firms could play a convening and educational role.** Audit chairs generally agreed that until final regulatory requirements are established, it is difficult to fully assess the role that external auditors and other practitioners will play in ESG reporting and assurance. But audit firms have specific expertise in reporting and applying standards and controls and could play an important role by *“pulling together companies in the same sector to navigate the alternatives allowed in various disclosure regimes, and to say which elections the companies will take. It will be a mess otherwise,”* a member said.
- **Questions remain about who will assure ESG information.** *“If audit committees end up with responsibilities for ESG reporting,*

### Leverage audit firm resources for education on ESG and other issues

External auditors often provide education on relevant accounting and audit issues. But members highlighted the need for broader education on ESG and other emerging issues, even though finding time to fit it into full calendars can be challenging.

For education on business risks and certain emerging issues, boards often look beyond the audit firm. *“But I also value and ask the audit firms for their insight,”* one member said. *“They often have well-written, well-researched papers that we can start with and then decide where the discussion needs to go.”* Another added, *“The full board could benefit from spending some time with a knowledgeable expert on ESG or other nonfinancial reporting issues such as cyber and artificial intelligence. I think you would have a much more aligned and informed board to help govern implementation of these things.”* Education can be useful on industry-specific topics or trends, which audit firms can usually benchmark. One member observed, *“Industry comparison is generally super helpful. It can be on a no-names basis but still tell you what’s happening.”*

*including attestation, which I expect they will,” one audit chair noted, “I don’t know whether my auditors are the best and most capable to do that or if it should be someone else.”* Another added, *“ESG reporting will involve a skill set that is not necessarily financial and will involve different technical capabilities, which will require a meeting of minds in what is reported.”* Members discussed the new skills that may be required on ESG engagements and noted the likely need for “upskilling” of engagement teams to support future workstreams. A member concluded, *“The profession will have to tell us what they can and can’t do in terms of the frameworks being developed to deliver assurance.”*

## About this document

The Audit Committee Leadership Network is a group of audit committee chairs drawn from leading North American companies committed to improving the performance of audit committees and enhancing trust in financial markets. The network is organized and led by Tapestry Networks with the support of EY as part of its continuing commitment to board effectiveness and good governance.

*ViewPoints* is produced by Tapestry Networks to stimulate timely, substantive board discussions about the choices confronting audit committee members, management, and their advisers as they endeavor to fulfill their respective responsibilities to the investing public. The ultimate value of *ViewPoints* lies in its power to help all constituencies develop their own informed points of view on these important issues. Those who receive *ViewPoints* are encouraged to share it with others in their own networks. The more board members, members of management, and advisers who become systematically engaged in this dialogue, the more value will be created for all.

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## Appendix 1: Participants

The following members participated in all or part of the meeting:



**Judy Bruner**  
Audit Committee Chair,  
Applied Materials and  
Seagate Technology



**Jeff Campbell**  
Audit Committee Chair,  
Aon



**Anne Drinkwater**  
Audit Committee Chair,  
Equinor



**Bill Easter**  
Audit Committee Chair,  
Delta Air Lines



**Bella Goren**  
Audit Committee Chair,  
Marriott International



**Robert Herz**  
Audit Committee Chair,  
Morgan Stanley and  
Fannie Mae



**Dagmar Kollmann†**  
Audit Committee Chair,  
Deutsche Telekom



**Arjun Murti**  
Audit Committee Chair,  
ConocoPhillips



**Ann Marie Petach**  
Audit Committee Chair,  
Jones Lang LaSalle



**Tom Schoewe**  
Audit Committee Chair,  
General Motors



**Tracey Travis**  
Audit Committee Chair,  
Meta



**Jim Turley**  
Audit Committee Chair,  
Citigroup



**Robin Washington**  
Audit Committee Chair,  
Salesforce

† Member of the European Audit Committee Leadership Network

EY was represented in all or part of the meeting by the following:



**Julie Boland**  
US Chair and Managing  
Partner and Americas  
Area Managing Partner,  
EY



**Linda Hill**  
Audit Partner, EY



**John King**  
Americas Vice Chair -  
Assurance, EY



**Pat Niemann**  
Americas Audit  
Committee Forum  
Leader, EY



**Norm Prestage**  
Audit Partner, EY



## Appendix 2: Reflection questions for audit committees

- ? How would you characterize the relationship with your external auditor? How could it be enhanced?
- ? What are good practices for building a strong working relationship with the external auditor?
  - o How do you build trust and foster open, candid dialogue while also balancing the need to maintain auditor independence?
  - o How often do you meet, both formally and informally? What topics do you focus on, especially in private sessions?
  - o How do you engage audit team members beyond the lead partner?
- ? How do you assess your external auditor's technology capabilities and learn what additional capabilities may exist?
- ? How do you leverage the audit firm to provide value beyond the core audit competencies?
- ? What questions do you have about your external auditor's capabilities in emerging areas, such as ESG?

## Endnotes

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<sup>1</sup> *ViewPoints* reflects the network's use of a modified version of the Chatham House Rule whereby names of members and their company affiliations are a matter of public record, but comments are not attributed to individuals or corporations. Italicized quotations reflect comments made in connection with the meeting by network members and other meeting participants.