

# *Our focus on audit quality*

2013 Report



**pwc**

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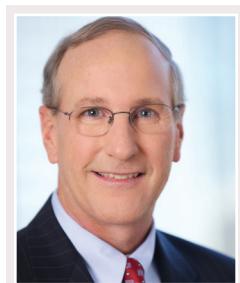
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# To capital market stakeholders



**Bob Moritz**  
US Senior Partner



**Vin Colman**  
US Assurance Leader

Please  
provide your  
feedback



We are interested in your views regarding this report. Please provide your feedback at [www.pwc.com/us/auditquality](http://www.pwc.com/us/auditquality).

We are pleased to provide you with our 2013 audit quality report. This is our third annual audit quality report, which continues to advance our goal of being transparent about how we deliver on our commitment to perform high-quality audits.

At PwC, we are proud of the quality of our audits. We view audit quality as a journey, rather than a destination, during which we are always striving to improve. Thus, each year we undertake a number of actions so that our audits continue to meet the challenges of increasingly complex accounting standards, evolving stakeholder expectations, regulatory input, and the highly competitive marketplace in which we operate. We describe in this report the actions we took during the year ended June 30, 2013.

This year, we have included in our report certain additional data about our audit practice and our investments in quality. Our intention in sharing this additional data is to enhance the transparency of our audit practice and our focus on quality. You can find our transparency data points by looking for the magnifying glass symbol  throughout the report.

The data points we have presented include information that some have suggested may be relevant to measuring audit quality. However, audit quality can mean different things to different people depending on the lens through which they assess quality. Thus, not all of the transparency data points we have presented may be directly relevant to audit quality. The Public Company Accounting Oversight Board has a project underway to develop audit quality measures that can provide insight into financial statement audit quality. We are

supportive of this effort and look forward to participating in the related dialogue. We will refine future audit quality reports to reflect the output of the project.

The companies whose financial statements we audit are increasingly doing business globally. Although this report relates to the US firm of PwC, we continue to focus on audit quality outside the United States by working with firms in the PwC global network to share our expertise on US accounting, auditing, and regulatory requirements. The strength of the PwC global network of firms facilitates our ability to meet the needs of the US capital markets.

This year we established the PwC Investor Resource Institute, which provides us with an opportunity to interact with members of the investment community outside the context of an audit. We believe the dialogue we will have through this forum will help us to identify ways to further improve the quality of our audits.

We have high expectations of ourselves, and we know that the public's expectation of us is similarly high. We also know that the role we have in the capital markets is an important one—audited financial information is essential to investor confidence and the effective functioning of the capital markets. We're proud of all of our partners and other professionals, who work hard to meet the responsibilities of this important role every day.

We are committed to maintaining our leadership position in promoting further improvements in auditing and financial reporting and performing the highest quality audits in the profession. To that end, our focus on audit quality is our highest priority.

# Our perspectives on audit quality

At PwC<sup>1</sup>, quality is—and always will be—our top priority. It's how we bring value to the capital markets.



There are many different views on what constitutes audit quality<sup>2</sup>. Feedback from regulators, investors, audit committees, and others help to inform our views on audit quality and how best to achieve it over the long term. Our view of audit quality focuses on our culture and values, and the infrastructure and processes we have in place to promote high-quality audits and the investments necessary to maintain them. To perform a high-quality audit, we follow certain basic principles:

- Comply with accounting, auditing, professional, and regulatory requirements, including independence
- Understand the companies we audit and the business environments in which they operate
- Use our expertise and resources to identify and resolve issues early
- Exercise integrity, objectivity, and professional skepticism

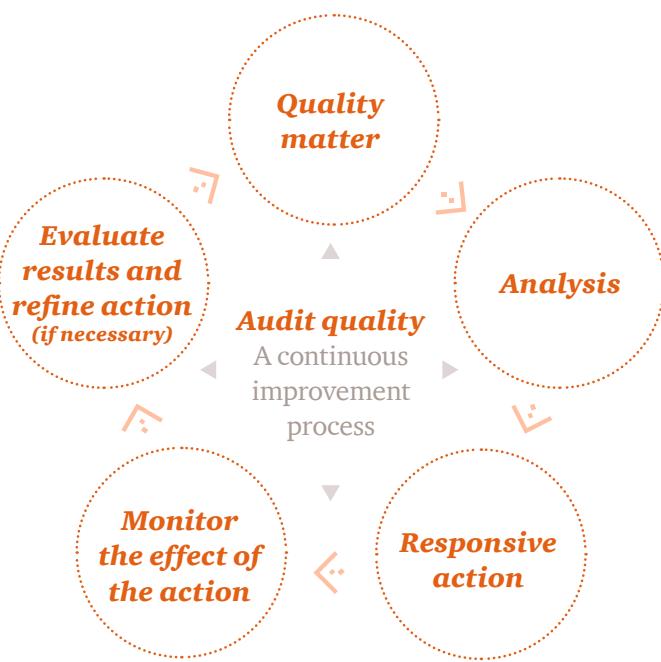
We reinforce these principles through individual practices that we believe are vital to perform a high-quality audit. The practices entail investing in relationships with management and audit committees, which promotes open communication and a greater ability to discuss difficult issues. They also include open communications within audit teams, staying current on professional standards, applying an objective and skeptical mindset, and taking personal responsibility for quality.

To sustain audit quality over the long term, we employ a continuous process of monitoring and evaluating numerous activities, for example, the amount of annual training completed by our professionals and the results of internal and external inspections of our audit practice. Then, we take action based on our evaluations, and continue to monitor and evaluate the effectiveness of these actions. This continuous process enables us to respond to an environment that is constantly changing and perform high-quality audits on a sustained basis.

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1 Throughout this report, the terms "PwC," "firm," "we," and "our" refer to PricewaterhouseCoopers LLP, the US member firm of PricewaterhouseCoopers International Limited (PwCIL). The member firms of PwCIL comprise the PwC global network.

2 "Audit quality is a complex subject and there is no definition or analysis of it that has achieved universal recognition." [International Auditing and Assurance Standard Board *A Framework for Audit Quality*, January 2013]



## Audit quality: A continuous improvement process

As the graphic above illustrates, we continuously assess the effectiveness of our improvement efforts in promoting sustained audit quality. We use various means to achieve this, including proactively monitoring our performance and seeking feedback from our people.

Throughout this report, we highlight areas where we've recently taken actions and made additional investments to promote audit quality. During the year ended June 30, 2013, these included:

- Continuing our emphasis on the review and supervision of audit work and the application of professional skepticism when conducting the audit
- Enhancing our audit policies and procedures so that we continue to provide the best guidance to our audit teams
- Developing and launching a new, progressive curriculum for our senior associates to enhance their auditing and accounting skills, and their skills in exercising professional skepticism, objectivity, and professional judgment

- Enhancing our internal inspections program, which facilitates audit quality improvements
- Establishing PwC's Investor Resource Institute to better engage with the investment community on matters of interest regarding audits and financial reporting, and to have the benefit of the investment community's feedback when contemplating audit quality enhancements

Our report describes these and other actions aimed at improving our ability to consistently perform high-quality audits.



### Looking for our transparency data points?

They can be identified by the magnifying glass symbol throughout the report. Data points 6, 8, and 9 cover our public company audit practice only. The remaining data points present information related to both our public and nonpublic company audit practices. All data points are presented with comparative figures.

# How our culture and values drive audit quality

Audit quality begins with our firm's tone at the top. Clear messages and actions from firm leadership combine with policies and programs to motivate high standards of individual behavior that drive audit quality.



## Tone at the top

Firm leadership<sup>3</sup> regularly conveys its expectations about audit quality to our partners and other professionals. This includes recognizing what we do well, emphasizing where we can improve, and providing examples of where we have held to our high standards of quality in the most difficult situations. These messages reinforce that audit quality is our top priority and make clear that the firm supports partners in standing firm in the name of quality.

Our quality messages are re-emphasized with our new partners when they are admitted to the firm internally and introduced to our new partners who are admitted from outside the firm. Quality messages are regularly communicated to all partners and other professionals through:

- Face-to-face meetings with partners in all of our markets
- Periodic e-mail communications

- Webcasts, internal social media, and town-hall meetings
- Learning and development programs
- Individual goal setting and performance evaluations

We periodically survey our professionals on the topic of audit quality on a confidential basis. Surveys provide insight into whether our quality messages are being consistently heard and understood. The results indicate that our people understand that our firm's top priority is audit quality and they have confidence that leadership will support them in holding to our high standards of quality. In fiscal year 2013, approximately 98% of our audit professionals who were surveyed reported that they received consistent messages about the importance of audit quality from both local and firm leadership.

## Accountability

Personal accountability is a key component of promoting audit quality. All levels of firm leadership, along with all of our professionals involved in the audit process, have a responsibility with respect to audit quality, and are expected to discharge their responsibility in the performance of their roles.

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*“One of the quality practices is to ‘take personal responsibility,’ so to me quality also means striving for continuous improvement.”*

—Assurance Associate

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<sup>3</sup> Please see the Appendix to this report for a description of the governance structure of the firm.

## **Leadership**

We provide all levels of assurance leadership with guidance on their responsibilities for audit quality, and how they will be accountable for them. This includes leaders of our audit practice in various regions, and of our market and industry groups.

Assurance leaders' key responsibilities for audit quality, depending on their roles, can include:

- Assisting audit partners in making key decisions that have quality implications
- Implementing and monitoring audit quality initiatives
- Overseeing our system of quality control
- Reviewing and monitoring partner workloads
- Recognizing and rewarding our people for audit quality
- Monitoring attendance at required training courses

## **Partners**

All assurance partners develop annual performance goals that reinforce their responsibilities for audit quality. The goals include any plans to remediate quality-related matters. The annual assessment process places specific emphasis on how well each partner has performed with respect to his or her goals in contributing to our quality objectives.

In fiscal year 2013, we accelerated our process to assess inspection results and identify causal factors. Using the output of that assessment, we then took steps that resulted in partners implementing a corrective action plan to address quality-related matters more quickly. This promotes greater accountability among our partners.

Partner income is based on a partner's level of responsibility within the firm, the firm's performance, and the partner's individual performance. Consistent with professional standards, our assurance partners are not compensated for selling non-audit services to companies whose financial statements they audit.

Quality is carefully considered in allocating partner income. Considerations include factors such as the results of internal and PCAOB inspections of completed audits, the timeliness of audit planning, and a demonstrated ability to stand firm on matters of quality. This applies to not just the lead audit partners, but also to quality review partners and assurance partners who contribute to audit quality by virtue of their specific leadership positions.

A partner's responsibilities may be reduced due to inconsistent audit quality. Quality-related matters can also result in a reduction in a partner's income. Partners who deliver exceptional quality are rewarded with additional income.

## **Non-partners**

Our annual assessment process captures information about how well each of our people has performed relative to our audit quality objectives. In fiscal year 2013, we began including a separate category for assessing an individual's "professional skepticism" to further stress this critical skill. Our non-partner professionals also participate in a performance bonus plan that is based, in part, on the achievement of audit quality.

When any of our non-partner professionals do not meet our audit quality objectives, this matter is considered in determining their annual performance rating, which affects future compensation and assignments. They also are required to develop a performance plan to promote personal improvement.

When senior managers and managers have primary review responsibility for areas where, based on inspection findings, our audit quality objectives were not fully met, they develop a corrective action plan similar to what we require of our partners. This plan is reviewed by a leader who has oversight of the individual and progress is monitored by the individual's partner advisor over the course of the fiscal year.

## Ethics, independence, and objectivity

### Ethics

Our code of conduct and supporting policies provide a set of standards that describe the behavior expected of our partners and other professionals. These standards provide guidance on how to conduct oneself under a range of circumstances. Various methods are available to our people to voice any concerns, including an anonymous ethics and compliance helpline and a confidential e-mail process.

The firm has strict written policies prohibiting the misuse of confidential client information. Additionally, we use various safeguards to protect confidential information. They include having policies that strictly limit access to non-public deals and other inside information to partners and other professionals on a need-to-know basis, and that require client data to be transferred using only firm-approved external storage devices, including encrypted USB devices. These policies are discussed in our training for new hires and reinforced for all of our people as part of annual training.

### Independence and objectivity

When we provide audit services, we require our professionals to be independent—in fact and in appearance—of the entity whose financial statements we are auditing. Being independent enables us to arrive at audit conclusions without being affected by influences that could compromise our professional judgment. It facilitates our acting with integrity and objectivity, and exercising

professional skepticism. It also helps to promote public confidence in the quality of our audits.

Being independent supports our culture, which entails conducting audits with a questioning mindset. Thus, it helps our professionals in asking difficult questions, challenging questionable accounting or disclosures, and standing firm in the name of audit quality. Our communications, independence training programs, and the actions and messages of leadership reinforce our commitment to integrity, objectivity, and professional skepticism.

### Partner and staff resources

The firm has 16 partners and approximately 200 staff dedicated to helping our professionals achieve and maintain independence. They issue independence policies and guidance, develop our annual independence training course, and develop and administer our compliance systems and procedures. They also serve as a resource for our people to consult with when resolving independence questions. For the twelve months ended June 30, 2013, the group engaged in over 17,000 consultations. In addition, it annually audits the independence compliance of selected partners and other professionals to assist them in maintaining their compliance and to monitor the firm's commitment to independence.

### Policy and systems

The firm's independence policy is based on the Code of Ethics for Professional Accountants of the International Ethics Standards Board for Accountants and supplemented to comply with the requirements mandated by US standard setters

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*“Quality is about asking questions and being professionally skeptical...not just stopping at Question 1 but having the courage to go on to Question 2.”*

—Assurance Senior Manager

and regulators (e.g., the Public Company Accounting Oversight Board (PCAOB) and the Securities and Exchange Commission (SEC)). We provide various technology-based tools to support our professionals in maintaining their independence, including systems designed to:

- Identify entities requiring independence
- Document the permissibility of proposed non-audit services
- Assess and monitor joint business relationships
- Initiate independence consultations
- Restrict, pre-approve, and monitor personal investments by partners and managers
- Document our professionals' annual confirmation of compliance with our independence policy

Our system to identify entities requiring independence promotes compliance by enabling the firm, our partners, and other professionals to monitor which entities they are prohibited from having financial and other relationships with. The system currently identifies over 245,000 companies for which our independence requirements apply.

Questions involving compliance are generally identified by the affected partner or other professional and through the firm's audits of individuals' personal independence compliance. When it is confirmed that a noncompliance matter exists, we address and resolve the matter promptly. Resolution includes discussing the matter with the audit committees of companies for which SEC and PCAOB independence requirements apply. In fiscal year 2013, we concluded, and the respective audit committees agreed, that none of the noncompliance matters we identified involving SEC and PCAOB independence requirements compromised our objectivity. Accordingly, none of those instances were of a nature that required us to resign (or caused the audit committee to ask us to resign) as the auditor.

### **Partner rotation policies**

Partner rotations provide an appropriate balance between maintaining our knowledge of the companies whose financial statements we audit and periodically bringing a "fresh look" to the audit. Our partner rotation system provides information that enables our assurance leaders to manage partner rotations appropriately and facilitates the transition of a new partner onto an audit engagement who has the right skills to maintain consistent audit quality.

In compliance with SEC and PCAOB requirements, lead audit partners and quality review partners on each public company audit rotate off of the engagement every five years. We also have rotation requirements for partners on non-public company audit engagements.

### **Training and confirmations**

Annually, all of our professionals receive training on the firm's independence policy and other compliance topics, including the appropriate handling of confidential information. When they join the firm, and at least annually thereafter, all partners and employees are required to confirm their compliance with all aspects of the firm's independence policy, and that they have not used any confidential information inappropriately. In addition, all partners confirm that any of the firm's business relationships for which they are responsible comply with the firm's independence policy.

### **Monitoring**

The firm's full-time Chief Ethics and Compliance Officer leads a team of compliance professionals that facilitates and monitors compliance with the firm's independence policy, along with other compliance requirements, such as CPA licensing and continuing professional education requirements. Each partner's compliance with the firm's personal independence requirements is generally audited every four years, while partners who comprise firm leadership are audited every two years. Employees are subject to audit periodically. A professional who violates our code of conduct or other firm policies is subject to disciplinary action, which may include dismissal.

### **Growth with a focus on quality**

Our strategy is to continue to grow the firm profitably through growth of both our assurance practice and our other professional services practices. Continued growth, particularly of services other than audits, contributes to our diversified and financially sound business and our ability to continue to invest in our people, our audit quality programs, and the other fundamentals of our business.

Our growth is achieved in carefully measured ways and with a focus on quality. For example, one of the factors we consider in deciding whether to accept a new audit engagement or renew an existing one is whether audit fees can be set at a level sufficient to support a high-quality audit. By using an effective audit methodology, leveraging technology and proprietary audit tools, and assigning partners and staff to an audit who have the appropriate skills and expertise, we can perform a high-quality audit at a reasonable cost.

We determine our audit fees based on the cost of the audit procedures necessary for a high-quality audit. When audit fees are set at an appropriate level, they should represent a fair reflection of the audit work that needs to be performed.

We then communicate the importance of setting fees appropriately to audit committees and management and help them understand the value we deliver—through high-quality audits that are performed efficiently, as well as by providing timely and relevant insights about their businesses.

At times, discussions about audit fees are challenging. We've made some difficult decisions to forego audit engagements where we've concluded that the fees do not fairly reflect the audit work to be performed, and we will continue to do so.

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*It's important that audit fees be sufficient to support a high-quality audit. But regardless of the fee, audit teams are expected to perform all audit work that is necessary for us to meet our audit quality objectives. We will not compromise audit quality for any reason.*

# **How we acquire and maintain the skills to perform high-quality audits**

The quality of our work is directly linked to the people we hire and how we support their development.



## **Human capital strategies**

### **Recruiting**

Our human capital strategies start with a rigorous recruiting program designed to bring in highly qualified candidates who have diverse backgrounds and skills. Our reputation enables us to attract the best talent at all experience levels. For example, we continue to be recognized as a “best place to work” by a number of different organizations in a variety of categories.

We actively seek out individuals who possess the specific skills, knowledge, and personal attributes we believe are necessary to perform high-quality audits. Consistent with our culture, we seek individuals who have a questioning mindset and intellectual curiosity, and demonstrate

courage and integrity. We also select individuals from diverse backgrounds and cultures to encourage fresh points of view and draw on their varied experiences. Our stringent hiring standards for entry-level and experienced professionals include assessing academic records and conducting background and reference checks.

### **Professional development**

To promote their development, we provide our professionals with increasingly challenging experiences and career opportunities. These may include tours with various practices within the firm and supporting our people when opportunities in different offices arise. We also recognize our non-partner professionals for career milestone successes and achieving the CPA or other relevant credential.

Becoming a CPA is an important part of our audit professionals’ career progression, as it demonstrates a mastery of core auditing and accounting knowledge. Passing the CPA exam is a significant step toward becoming a CPA, and in our firm is a prerequisite for advancement to the audit senior associate level.

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*In 2013, 11 of the 39 individuals recognized by the AICPA for achieving exceptional results on the CPA exam were from PwC, the highest number from any of the accounting firms.*

Average annual voluntary turnover rate		
	FY13	FY12
Senior Manager/Manager	13.5%	12.6%
Senior Associate	23.1%	21.5%
Associate	15.9%	13.4%

Average annual hours worked over 40 hours per week (2,080 annually)		
	FY13	FY12
Partner	495	494
Senior Manager/Manager	401	410
Senior Associate	356	364
Associate	312	334

## Retention

The retention of highly qualified people is an important way for us to maintain sufficient resources to achieve sustained audit quality. Public accounting provides opportunities for rapid professional growth that can prepare individuals for varying responsibilities, including with other organizations. For example, many of our professionals leave to take key accounting and financial reporting roles where they continue to make important contributions to the functioning of the capital markets. Accordingly, turnover rates for the public accounting profession are typically higher than the turnover rates for accountants outside of public accounting. Our goal is to achieve rates of turnover for our assurance senior managers and managers, senior associates, and associates that generally do not exceed 11%, 21%, and 15%, respectively. 

One way we focus on retention is by increasing the flexibility our people have to better balance their professional and personal lives. As professionals, our people work the hours it takes to meet their responsibilities. The hours worked can vary based on a variety of factors. For example, the scope of an audit can increase due to an acquisition, complex business transactions, new systems, and new financial reporting standards. Over the past five years the average annual hours worked by our audit professionals over 40 hours per week (2,080 annually) have ranged from 273 hours for associates to 510 hours for partners. 

We have processes designed to help our people properly manage their workloads, especially during peak periods when significantly more hours may be incurred. These include periodically reviewing hours worked with a goal of providing our people with sufficient capacity to perform their audits.

## Learning and development

At PwC, a significant amount of learning occurs through on-the-job review and supervision, and through mentoring. For example, members of our audit teams learn to exercise professional judgment by watching more senior professionals (i.e., partners and managers) interact with management and audit committees and resolve issues. They also see how objectivity and professional skepticism are exercised, and learn the importance of asking the right

questions and conducting appropriate follow-up during an audit. In general, how we perform our audits, the composition of our audit teams, and the opportunities we provide our younger partners to work with more senior partners on their engagements, promote meaningful on-the-job training. The time our partners and managers spend on average on an audit in relation to the time spent by others on the team also promotes learning opportunities for our people.  3

Our audit professionals also hone their skills through participation in firm-developed learning and development programs. They are required to comply with continuing professional education (CPE) requirements mandated by the firm, and, if they are CPAs, any additional requirements mandated by the states where they are licensed. On average our professionals earn significantly more CPE credit hours than the 120 hours required by the firm over a three-year period. Further, professionals performing audit or assurance work in certain specialized industries must meet specific industry-focused CPE requirements. The firm's Ethics and Compliance office administers processes that promote compliance with all CPE requirements.  4

We require our audit professionals to attend various firm-developed audit training courses. Attendance at required training courses is an important component of an individual's performance assessment, and is monitored by locally based assurance leaders. In addition, virtually all required audit and accounting training courses are followed by learning assessments. These assessments help extend the learning experience by testing knowledge gained during the course, and providing participants with a better understanding of where they could improve.

Our training courses include a significant focus on audit and accounting skills, as well as business and industry developments, and are tailored to the experience level of our professionals. In fiscal year 2013, we redesigned our senior associate training curriculum. This was a continuation of an initiative we began last year, when we updated our training curriculum for entry-level professionals and associates (those with one to three years of experience). The updated

	FY13	FY12
Partner to manager	1 to 3.6	1 to 3.5
Manager to staff	1 to 4.2	1 to 4.2
Partner to staff	1 to 18.7	1 to 18.4

	FY13	FY12
Average CPE credit hours earned by our professionals over a three-year period in excess of 120 hours	77	71

senior associate curriculum includes a one-week, in-person training course with an audit simulation designed to provide realistic examples of how to exercise integrity, objectivity, and professional skepticism throughout the audit.

Our assurance learning and development group is led by an audit partner, with targeted support provided by audit partners who have specialized industry and technical expertise. Together with approximately 25 other experienced audit and education professionals, the group develops our assurance training courses.

In developing the content for our training courses, we draw upon various resources, including:

- Results of both internal and external (for example, PCAOB) inspections of our audit practice (refer to pages 20–23)
- Observations from our Chief Auditor Network (refer to page 18)
- Focus groups, surveys, feedback, and other information to identify the areas where additional training would be beneficial
- Results of post-course learning assessments completed by participants of our required technical courses to measure the extent to which they absorbed the teachings in the course

In addition to our formal training courses, our professionals receive regular updates on accounting and auditing matters through various National office and industry group communications.

# How our infrastructure supports audit quality

Performing high-quality audits requires an infrastructure and processes that support audit quality.



## Audit methodology and processes

### ***Considerations in undertaking an audit engagement***

While our business model seeks to grow our audit practice, we remain selective in accepting new audit engagements and renewing existing ones. We will not sacrifice audit quality for any reason, including additional revenue.

We require an assessment to be performed whenever we are considering providing assurance services, including audits, to an entity for the first time. Such an assessment focuses on information about the company and its key personnel. It also includes identifying the potential risks associated with an engagement, ascertaining whether mitigating actions can reduce those risks, and linking those actions to our audit plan.

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*“Quality...never leaves our thought process. We ask ourselves a lot of questions throughout the audit to keep quality top of mind.”*

—Assurance Partner

We assess whether we have the resources with the right skills, experience, industry knowledge, and capacity to perform a high-quality audit in light of the identified risks. We accept only audit engagements for which we believe our audit procedures can satisfactorily address the risk of material financial statement misstatement, whether due to error or fraud, and that align with our strategies for growing our practice.

The risks posed by any existing audit engagement may change for various reasons, including changes in the entity's management, new business ventures, adverse business conditions, or integrity issues. Accordingly, after acceptance we assess audit engagements annually or sooner if a significant event occurs, to determine whether to continue the audit relationship.

### ***Methodology, tools, and processes***

To promote consistent audit engagement performance, the PwC global network of firms (refer to page 19) agree to follow a baseline audit methodology. We supplement the methodology through the development and enhancement of audit tools and related guidance that are specific to the needs and requirements of the US firm.

The identification and evaluation of audit risks is a central feature of our audit methodology. Under our approach, we seek insights into the business, the risks inherent in that business, and the related financial reporting and audit risks. Those insights enable us to design and conduct more effective and efficient audits and more effectively communicate with audit committees and management.

To audit effectively in a changing environment, we continually supplement our audit methodology, tools, and processes with a focus on improving both the effectiveness and efficiency of our audits. This includes enhancements and supplemental guidance to promote consistent interpretation and application of auditing standards, particularly in unique situations. We often look to our monitoring results to identify which auditing standards to focus on in this regard.

As part of our recent improvement efforts, we increased our focus on supervision, review, and documentation of reviews by the audit partner, quality review partner, and other experienced professionals. We also provided enhanced tools and guidance through a series of communications and required training and through updates of our audit software.

We believe enhanced standardization will promote further improvements in audit quality. Thus, our efforts in fiscal year 2013 continued to focus on embedding best practices in our processes, tools, and templates.

Fiscal year 2013 enhancements focused on:

- Entity-level and management review controls
- Sources of potential misstatement
- Expediting audit planning, allowing for increased focus on execution and supervision
- Enhancing review and supervision techniques, such as coaching others in the use of professional skepticism

- Evaluating key assumptions used in developing accounting estimates
- Planning and scoping multi-location audit engagements
- Using the work of others
- Enhancing the scope of review required by senior members of the audit team

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*“The foundation of quality is performing an audit in accordance with the professional standards... Quality is embedded in everything we do, every day of the year.”*

—Assurance Manager

We're increasing the use of documentation tools that provide a consistent framework for documenting audit evidence, and we've clarified, simplified, and eliminated duplication in our standardized procedures.

We continue to leverage our Global Assurance Delivery Model, under which certain audit activities are performed by audit team members who are located in one of three centralized service centers, two of which are outside of the United States. This promotes more consistent execution and provides our locally based audit teams with additional time to focus on other aspects of our audits. In fiscal year 2013, our service centers performed nearly 1 million hours of audit activities, approximating 6% of audit hours. Our goal is to increase the utilization of our service centers in fiscal year 2014 and beyond.

### ***Audit committee communications***

We believe effective oversight of auditors by audit committees is one of the keys to promoting greater audit quality. Thus, we are supportive of a robust dialogue between auditors and audit committees, as both benefit from timely, meaningful, and direct exchanges of information about the audit.

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*The understanding we gain of a company's business through our audits enables us to identify issues that are important to audit committees and management. This facilitates our ability to bring value by sharing insights on emerging trends and leading practices, which can help management improve financial reporting, operations, controls, and other aspects of the business.*

The dialogue we engage in with audit committees enables them to more effectively execute their oversight role. This dialogue may include obtaining their views on financial reporting risks and areas that warrant audit attention, discussing the audit resources to be allocated to the audit, and whether the audit fee fairly reflects the audit work to be performed.

Our audit teams communicate with audit committees of public companies on at least a quarterly basis (often more frequently). Communications include at least annual discussions about our independence and a discussion of our role and the role of management. In addition, as required by PCAOB rules, we issue a written communication to the audit committee about matters that could reasonably be thought to bear on our independence.

The audit committee approves our audit engagement and related audit fee and, when applicable, non-audit engagements and related fees. The nature and extent of other

communications varies based on the facts and circumstances. For example, our communications could include sharing the perspectives we gain from our audit on the quality of the company's personnel, the effectiveness of its systems, the likelihood and impact of cyber threats, and other matters that are unique to the company. We may also engage in a dialogue with audit committees regarding their oversight of the audit and their governance role generally.

At a minimum, we discuss with audit committees annually the following matters specific to their audits:

- Critical accounting policies and acceptable alternatives discussed with management
- Material written communications with management
- Significant management judgments and accounting estimates
- Significant risks and exposures
- Any significant deficiencies and material weaknesses
- Any material uncertainties related to events and conditions that may cast doubt on the company's ability to continue as a going concern
- Any fraud or illegal acts

Because of the importance of the audit committee to audit quality, we are committed to discussing with the audit committee the results of the PCAOB's inspection of our audit of the company's financial statements and trends from other PCAOB inspections that may have a bearing on current and future audits. We also share information about how we continually improve audit quality, such as leveraging the results of our internal inspections and providing targeted training.

**5**

**Ratio of partners serving in technical support roles to the total number of audit partners**

FY13  
1 to 6.5FY12  
1 to 7.2

## Resource management

Reviewing and monitoring partner responsibilities is an important process that contributes to our ability to perform high-quality audits. This includes aligning partner roles with partner capacity, and providing partners with sufficient time to effectively review the audit work and supervise the engagement. It also focuses on a partner's tenure, capability, and industry experience. During fiscal year 2013, we continued to enhance this process to more effectively monitor our partners' workloads.

The process begins by capturing information about each assurance partner's audit and non-audit responsibilities at the beginning of the fiscal year. This information is evaluated by market and regional assurance leaders, as well as regional and national risk management partners. Audit partner responsibilities are then monitored, including a mid-year update, to assess whether, as circumstances change, partners continue to have the capacity and capability to perform high-quality audits. Partners are also encouraged to initiate a dialogue regarding any potential capacity or capability issues.

An increased number of assurance partners in our firm helps facilitate a more balanced workload for our partners, which increases our ability to consistently perform high-quality audits. During the year ended June 30, 2013, we announced 56 internal partner admissions to our assurance practice, resulting in a net increase of 28 partners after considering partners who retired as of that date.

## Consultation process and use of specialists

As part of our collaborative culture, our audit teams are expected to leverage the full quality support network of the firm when accounting, auditing, and financial reporting matters arise. A number of partners and other professionals are devoted to supporting audit partners in performing high-quality audits. 5

In addition to those who provide technical support (National office and Chief Auditor Network), the firm's infrastructure that supports audit quality includes risk management partners, quality review partners, and market and industry group leaders. In reaching conclusions, especially on some of the most difficult aspects of an audit, the audit partner and individuals from those groups, as applicable, will have an opportunity to align their views before decisions are conveyed to the audit committee and management.

Partners and other professionals who provide consultation support also assist audit teams in reviewing the assessments performed by management and audit committees of errors that are identified in previously issued financial statements. Such assessments may result in a conclusion to restate those financial statements. 6

**6**

**Number of restatements as a percentage of issuer\* audit clients**

FY13 1.15% (21 out of 1,825)

FY12 0.80% (15 out of 1,870)

\*For purposes of this report, "issuer" audit clients comprise SEC registrants and mutual funds.

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*The National office provides regular updates on accounting, auditing, and financial reporting matters, including quarterly webcasts and weekly communications, to help our people learn about these important matters and how they affect the design and execution of our audits.*

### **National office**

The National office collaborates with audit teams to promote high-quality financial reporting. The partners and other professionals in our National office have expertise in accounting, auditing, SEC, and financial reporting matters. They regularly advise audit teams on significant, unusual, and complex matters in these areas. They also play a role in establishing firm policies that address these matters.

Under our consulting protocol, there are specific matters for which consultation with our National office is required (for example, when evaluating the severity of a potential material weakness in internal control that is remediated close to year-end). Required consultations are intended to promote consistency in how we approach and resolve audit issues.

Audit teams are encouraged to consult on other matters as warranted by facts and circumstances. In the event an audit partner disagrees with the advice provided by our National office, a resolution process provides guidance for elevating the discussion until the matter is satisfactorily agreed upon and resolved collectively.

### **Risk management**

PwC's risk management structure includes more than 100 experienced partners in national, regional, and local roles who devote time to risk management activities. Audit teams are required to consult with a risk management partner on specific issues, such as certain materiality, error identification and resolution, principal auditor, and going concern matters. Our risk management partners also help audit teams assess risk on both

a qualitative and quantitative basis in determining whether to undertake or continue an audit engagement.

### **Chief Auditor Network**

Our Chief Auditor Network provides locally based support for our audit teams. The partners and other professionals in the network have a strong connection to our National office audit experts. The Chief Auditor Network's primary purpose is to provide auditing advice, including through reviews of certain aspects of an audit engagement before the audit is completed, leveraging the deep expertise of the professionals in the network on auditing standards, policy, and methodology. This support helps our audit teams to identify where specific audit attention may be warranted, design effective and efficient audit procedures, and exercise professional skepticism.

The professionals in the network participate in market and industry group meetings, sharing knowledge about frequently asked questions and areas that merit additional focus. They also contribute to the development of course content for our required audit training, and serve as instructors for many of the courses.

### **Quality review partner**

We assign a quality review partner to our public company audit engagements, and certain other audits. These are partners who have sufficient and appropriate technical expertise and experience to perform effectively in the quality review partner role. The quality review partner's responsibilities include reviewing the audit plan, considering the firm's independence, and discussing the significant risks identified by the audit

team and the responses to those risks. The quality review partner also reviews certain accounting, auditing, and financial reporting matters, and the financial statements and related disclosures. When a restatement of previously issued financial statements is being considered by the audit partner to correct a potential error, the matter is first discussed with the quality review partner.

### **Other specialists**

To improve audit quality, the firm has subject matter experts who assist audit teams in considering key matters in specialized areas. These include, for example, valuation, tax, information technology, and actuarial matters.

By leveraging the knowledge of our specialists, we can better understand industry trends and emerging risks that have a bearing on our audits. We can also better evaluate complex transactions, assess accounting treatments, and identify areas where additional professional skepticism may be warranted. In particular, our information technology professionals are integral to helping our audit teams understand complex internal control systems. In fiscal year 2013, specialists comprised approximately 10% of total audit engagement hours.

### **Global network**

The firm is a member of PricewaterhouseCoopers International Limited (PwCIL), a UK private company limited by guarantee. The member firms<sup>4</sup> of PwCIL are from more than 150 countries and together form the PwC global network. Member firms can use the resources and methodologies of the network and seek to secure the provision of professional services by other member firms. As a member of the PwC global network, we are able to serve companies across borders and regions and in emerging markets around the world.

The network promotes audit quality in the following ways:

- Develops and implements policies to achieve a common and coordinated approach among member firms regarding quality

- Provides processes, tools, and resources to assist member firms in meeting the network's quality standards
- Maintains a global audit methodology
- Develops and provides training and audit tools
- Coordinates resources to perform quality reviews of member firms
- Assists member firms in enhancing their supporting infrastructure to promote audit quality
- Monitors member firms' audit quality to help identify areas for improvement

Our assurance leader is a member of the network's global assurance leadership team. This team focuses on quality-related matters throughout the network and makes suggestions on how to address them.

Each member firm is responsible for monitoring its quality control system. This includes reviewing the quality of its management level controls and the audit work it has performed. A network team monitors that review. When issues are identified, the member firm prepares a remediation plan and the network monitors its implementation.

Performing audits in emerging and rapidly growing markets can present challenges because of factors such as culture, less-developed company governance practices, and limited resources. Our audit partners understand their responsibilities for quality and address these challenges through various means which, in addition to effective oversight of the audit work, may include visits with the audit teams of other member firms. At a member firm level, these challenges may be addressed through secondments of experienced professionals to other member firms.

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4 Each member firm is a separate legal entity. Please see [www.pwc.com/structure](http://www.pwc.com/structure) for further details.

# How we know our teams execute high-quality audits

To achieve sustained audit quality, we monitor our performance, learn from our experiences, and continuously make improvements to enhance the quality of our audits.



## Reviews of in-process audit engagements

In fiscal year 2013 and 2012, professionals in our auditing services group and Chief Auditor Network reviewed a number of audit engagements prior to the issuance of our audit reports. The reviews primarily focused on specific elements of the audit plans for those engagements. 

Also in fiscal year 2013, our inspections group subsequently selected approximately fifty of those audit engagements and, prior to

FY13 **300**  
FY12 **280**

Approximate number of in-process audits reviewed

the issuance of our audit reports, performed targeted reviews that focused on providing audit teams with feedback on their audits. These reviews generally considered how recent policy and methodology enhancements were applied. The interactions that occur between the reviewers and our audit teams through these types of monitoring activities help our audit teams to execute some of the more complex areas of our audits. However, they are different than internal inspections, which are performed after the issuance of our audit reports, and are discussed below.

## Internal inspections of our audit practice

Our inspections group comprises a core group of partners and other experienced audit professionals who are committed full time to internal inspections. The core group is assisted by members of our Chief Auditor Network and other audit partners and experienced audit professionals who commit a portion of their time to inspections.

Our inspections group inspects completed audit engagements, which are selected to achieve broad coverage of our audit practice. They analyze the inspection results by considering whether our audit quality objectives were fully achieved. If they were not, the group considers the potential causes and works with our auditing services group, Chief Auditor Network, audit methodology group, learning and development group, and firm leadership to determine whether additional guidance or training, modifications to our audit methodology, or targeted messages from leadership

are needed. The information we obtain from internal inspections contributes to our continuous learning cycle.  8

We estimate that the partners and other professionals in the inspections group will spend approximately 80,000 hours conducting our 2013 inspections (of over 300 public and private company 2012 year-end audits) and targeted reviews. When combined with assistance from experienced audit partners and other senior audit professionals, we estimate we will spend approximately 100,000 hours conducting our 2013 inspections and targeted reviews.

Our inspections group annually evaluates the firm's system of quality control of our audit practice. Our system addresses (i) leadership's responsibility in their roles for quality, (ii) relevant ethical requirements, (iii) considerations in undertaking an audit engagement, (iv) human capital needs, (v) engagement performance, and (vi) our process for monitoring the effectiveness of our quality control policies and procedures. Our system is also subject to annual review by professionals from the PwC global network. The most recently completed annual evaluation confirmed that our system of quality control is functioning effectively.

The results of our 2012 internal inspections of selected 2011 audits indicate that we have improved how we utilize substantive analytic procedures, and our audit procedures related to financial instruments. These areas were identified for improvement as part of our (and the PCAOB's) inspections of selected 2010 audits. Based on our 2012 internal inspections, we continue to focus our improvement efforts on auditing estimates and fair value measurements, internal control over financial reporting, and income taxes, areas that the PCAOB also identified in its inspections.

The purpose of our inspections group is to identify areas where we can improve. Because auditing is a complex and judgmental process and the evolution of auditing standards is ongoing, we expect the group will continue to identify new areas for improvement. In this



way our inspections group helps us to maintain a mindset of continuous improvement. As a result of our 2012 internal inspection process, we have focused certain of our quality improvement efforts on the following areas:

- Identifying internal controls, testing thresholds, and the impact of segregation of duties conflicts relevant to testing journal entries; documenting journal entry selection criteria and testing results to determine whether the objective of the test (typically evaluating fraud risk) is met.
- Consistently documenting (i) independence discussions with audit committees about potential effects of proposed tax services and (ii) independence assessments when the client acquires a non-audit client or the board, officers, or significant shareholders change.
- Evaluating a company's business process "end to end," identifying likely sources of potential misstatements; evidencing discussions with the company/audit committee about risks of material misstatements, including the risk of fraud and error, as part of audit planning.
- Evidencing effective and timely review by the quality review partner and appropriate supervision and review of the work of tax specialists.

## External inspections of our audit practice

### PCAOB inspections

The PCAOB inspects our public company audit practice annually to identify areas for improvement. Using a risk-based inspections approach, which is designed to identify audit engagements that are most likely to have issues, the PCAOB inspected 63 and 54 of our audits of issuer financial statements for 2011 and 2012, respectively.

## Understanding a PCAOB Inspection Report

- Comprises public (Part I) and non-public (Part II) portions
- The PCAOB refers to engagement-specific inspection findings as “deficiencies”<sup>5</sup>
- The PCAOB uses the term “audit failure” to describe a situation where it has determined that not enough evidence was gathered to support the audit opinion
- Audit failure does not mean the PCAOB has concluded that there is a material misstatement in the financial statements
- The PCAOB notes that inspection reports should not be used as a gauge for assessing the overall quality of a firm’s audit practice and are not intended to be balanced report cards or overall ratings tools

There is a high degree of judgment involved in the inspection process, both on the part of the PCAOB’s inspectors to reach their conclusions and by us in evaluating their conclusions. In many cases we agree with the PCAOB inspectors’ assessment of our work. In all cases, we take their observations into account in our ongoing audit quality improvement efforts.

### Part I of a PCAOB report

Part I of our 2011 inspection report (dated September 27, 2012) and Part I of our 2012 inspection report (dated August 20, 2013) cover inspections of selected 2010 and 2011 year-end audits, respectively.  In the spring of 2011, we began taking a number of bolder steps to improve our ability to consistently perform high-quality audits, as first described in our 2011 report *Our focus on audit quality*.

Consistent with the areas highlighted in our 2011 and 2012 Part I, we continue to focus our improvement efforts on the following:

- Auditing internal controls over financial reporting and testing those controls in a financial statement audit
- Testing measurements and disclosures of the fair value of “hard-to-value” financial instruments and items other than financial instruments, including acquired assets and liabilities
- Testing management’s process and assumptions for estimates and fair value measures, such as inventory valuation, inventory reserves, warranty reserves, loss contingencies, loan loss reserves, tax provisions, and goodwill impairment
- Designing and performing substantive analytical procedures (identified primarily in 2011 inspections)
- Using the work of other auditors, including internal auditors (identified primarily in 2011 inspections)

### Part II of a PCAOB report

Part II of a PCAOB report contains the PCAOB’s criticisms of a firm’s system of quality control and reflects its review of certain of a firm’s practices, policies, and processes related to audit quality. In reviewing these, the PCAOB considers its engagement-specific findings identified in Part I. Thus, its Part II comments often address a firm’s practices, policies, and processes in the context of its specific Part I findings. The Part II review generally focuses on:

- Management structure and processes, including the tone at the top

	Audits inspected	Audits included in Part I	9
2012	54	21	
2011	63	26	
2010	75	28	

5 In its report, the PCAOB notes that “...any deficiency observed in a particular audit...does not reflect any determination by the Board as to whether the Firm has engaged in any conduct for which it could be sanctioned....”

- Practices for partner management, including allocation of partner resources and partner evaluation, compensation, admission, and disciplinary actions
- Policies and procedures for considering and addressing the risks involved in accepting and retaining clients, including the application of a firm's risk-rating system
- Processes related to a firm's use of audit work that its foreign affiliates perform on the foreign operations of a firm's US issuer audit clients
- A firm's processes for monitoring audit performance, including processes for identifying and assessing indicators of deficiencies in audit performance, independence policies and procedures, and processes for responding to weaknesses in quality control

If a firm has addressed, to the PCAOB's satisfaction, the quality control matters described in Part II within twelve months after it is issued, no portion of Part II is made public by the PCAOB. In 2013, the PCAOB informed us that while it believed we satisfactorily addressed the majority of its criticisms in Part II of our 2008 and 2009 inspection reports (covering audits of 2007 and 2008, respectively), it was not satisfied with the steps we took to address certain criticisms within the respective 12-month periods. Accordingly, the PCAOB made public those portions of Part II for those years; they are available on the PCAOB's website.

### **Part II – 2008 and 2009**

The PCAOB inspected 50 audits in 2008 and 76 audits in 2009. Its criticisms with respect to those inspections centered on three general areas: (a) estimates; (b) fair value measurements; and (c) reliance on controls/using the work of others, including general observations related to those areas regarding professional skepticism, due care, supervision, and review.

These involve some of the most complex, judgmental, and evolving areas of an audit. This is consistent with the matters typically addressed in Part II. The PCAOB states that its criticisms "are not intended to result in conclusive findings" and "[do] not signify anything

about the merits of any additional efforts a firm may have made to address the criticisms after the 12-month period" following issuance of a Part II.

The actions we took during the applicable 12-month periods for 2008 and 2009 included (i) issuing new audit tools and guidance, (ii) providing additional targeted training, (iii) enhancing our engagement review requirements overall and in specific areas, (iv) assessing and adjusting partner workloads as needed, and (v) creating a tool that reminds our professionals of relevant principles and considerations when applying professional skepticism. Our improvement efforts are ongoing, however, and are not confined to any one 12-month period following issuance of an inspection report.

We believe our actions in response to the Part II comments were significant; however, we acknowledged the PCAOB's determination with a view toward continued cooperation with the board and a furtherance of our ongoing commitment to audit quality.

The PCAOB has determined that it is satisfied with the actions we took to address its observations in Part II of our 2010 inspection report (covering our 2009 year-end audits). For Part II of our 2011 inspection report (covering our 2010 year-end audits), the applicable 12-month period ended on September 26, 2013. For Part II of our 2012 inspection report (covering our 2011 year-end audits), the applicable 12-month period ends on August 19, 2014.

### **Other reviews**

An inspection of our private company audit practice (a peer review) is performed every three years. Our latest peer review was completed by Grant Thornton LLP in December 2012. A total of 83 engagements were inspected. The system of quality control for our assurance practice was also evaluated. Firms can receive a rating of pass; pass with deficiencies; or fail. We received a rating of "pass." Our employee benefit plan audit practice was also recently inspected by the US Department of Labor and that inspection produced similarly positive results.

## How we share insights with the marketplace

Our focus on audit quality includes being actively involved in developing the profession's perspectives on events in the audit, financial reporting, regulatory, and business environments.



### Professional and regulatory

Our role in the capital markets provides us with a unique perspective of companies' businesses and their financial reporting. We also have significant insight into the thinking of other stakeholders in the capital markets—regulators, investors, standard setters, policymakers, academics, and others—about financial reporting. We use this knowledge to inform our thinking and, within the bounds of confidentiality restrictions, share that knowledge through participation in debates and discussions aimed at improving audit and financial reporting quality.

Through our various publications, we share with stakeholders our views on issues that could affect audit quality. We also meet with policymakers, regulators, and standard setters to share our perspectives. And, we respond to various proposals by submitting comment letters and participating in public meetings.

Another way our firm promotes audit quality in the marketplace is through our involvement in the Center for Audit Quality. The Center for Audit Quality's governing board includes the chief executive officers of the largest auditing firms (the board is currently chaired by our firm's Senior Partner). Its activities are aimed at improving audit quality, with recent activities focused on identifying components of a definition of audit quality and the most relevant audit quality indicators.

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*To learn more about our perspectives, please visit [www.cfodirect.com](http://www.cfodirect.com)*

### Audit committees

Through our Center for Board Governance, we contribute to increased audit and financial reporting quality for the benefit of the capital markets. We do this in part by assisting corporate directors to more effectively meet the challenges of their oversight roles. For example, we encourage audit committees to actively oversee the work of their auditors, evaluate auditor performance, and challenge the auditor's judgments.

We also provide information to audit committees on significant corporate governance and financial reporting developments through a series of publications, available on our Center for Board Governance website<sup>6</sup>. And, we engage with audit committees and share our insights through seminars, roundtables, webcasts, and one-on-one meetings.

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<sup>6</sup> [www.pwc.com/us/en/corporate-governance/about-the-center.jhtml](http://www.pwc.com/us/en/corporate-governance/about-the-center.jhtml)



## Investment community

As the needs and expectations of the capital markets evolve, we believe it is important for us to engage with the investment community. PwC's Investor Resource Institute, which we established in fiscal year 2013, creates opportunities for us to meet with, listen to, and learn from the investment community.

Through the Institute, we can share our insights on many issues of interest to the investment community, including topics that are relevant to accounting and auditing as well as those involving our broader market perspectives (such as current risks in cybersecurity and the potential resurgence of the US manufacturing sector). In turn,

we can obtain a deeper understanding of investors' views on a wide variety of topics, such as their perspectives on the rules that govern financial statement disclosures. Since its inception, we have benefited from a rich dialogue on these and similar matters with investor groups and look forward to an ongoing exchange of information.

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*To learn more about the PwC  
Investor Resource Institute,  
please visit [www.pwc.com/us/  
InvestorResourceInstitute](http://www.pwc.com/us/InvestorResourceInstitute).*

# Appendix: Legal and governance structure of the firm

## **Legal structure and ownership of the firm**

The firm is a limited liability partnership established under the laws of the State of Delaware. All interests in the firm are held by its partners and principals<sup>7</sup>, all of whom are individuals.

## **Governance structure of the firm**

The firm's Senior Partner serves as Chairman and Chief Executive Officer and manages the firm. The Senior Partner may appoint persons and committees to assist with firm management and provides the Board of Partners and

Principals, which is PwC's governing body, with initiatives for the firm's philosophy, policies, and direction.

To assist him in discharging his responsibilities, the Senior Partner has appointed a Leadership Team, which works with him in managing the firm. The responsibilities of the Senior Partner and the Leadership Team include establishing and determining the effectiveness of the firm's system of internal control, including those relating to the quality of the firm's audit services. All of the members of the Leadership Team are partners or principals. Changes to the Leadership Team are determined by the Senior Partner. The Senior Partner is elected by a partner vote for a four-year term that can be renewed once.

### Members of the Leadership Team as of the date this report was issued

Chairman and Senior Partner	Robert Moritz, CPA
Markets, Strategy and Stakeholders Leader and Vice Chair	Tim Ryan, CPA
Services Leader and Vice Chair	Dana McIlwain, CPA
Assurance Leader and Vice Chair	Vincent Colman, CPA
Tax Leader and Vice Chair	Mark Mendola, CPA
Advisory Leader and Vice Chair	Miles Everson
Network Alignment and Vice Chair	Mitchell Cohen, CPA
Markets and Sectors Leader and Vice Chair	William Cobourn, Jr., CPA
Network and US Transformation Leader and Vice Chair	Michael Burwell, CPA
Chief Financial Officer and Vice Chair	Carol Sawdye, CPA
Human Capital Leader and Vice Chair	Terri McClements, CPA
Chief Diversity Officer	Maria Castañón Moats, CPA
General Counsel and Chief Risk Officer	Diana Weiss
Marketing and Sales Leader	Robert Gittings, CPA
Regulatory Affairs and Public Policy Leader	Laura Cox-Kaplan
Chief Administrative Officer and Partner Affairs Leader	Gary Price, CPA

## **Board of Partners and Principals**

### **Authority**

The Board is responsible for approving the overall strategic direction of the firm. It approves long-range strategies and business plans, and major transactions that could significantly affect the firm's business. Its authority also includes the approval of the firm's capital policies, the manner in which partners participate in firm profits, and the admission of partners. It approves the compensation of the Senior Partner and members of the Leadership Team as a group, after a review and recommendation by a committee of the Board. All candidates proposed by the Senior Partner nominating committee to stand for election as Senior Partner must also be approved by the Board.

<sup>7</sup> A partner is a certified public accountant (CPA) whereas a principal is not. Only CPAs may sign an audit opinion. Partners and principals are alike in most other aspects of the partnership, such as sharing in profits/losses, managing risk, developing our staff, investing in client relationships, and performing services for clients. For purposes of this Appendix, "partner" refers to both partners and principals.

### Members of the Board of Partners and Principals as of the date this report was issued

Robert Moritz, CPA <i>Chairman and Senior Partner</i>	
Brian Cullinan, CPA <i>Lead Director</i>	James Kolar, CPA
Thomas Archer, CPA	John Livingstone
Brendan Dougher, CPA	Karen Lohnes
John Farina, CPA	John Maxwell, CPA
Saverio Fato, CPA	John McCaffrey, CPA
Julie Harmon, CPA	Jacqueline Olynyk, CPA
Linda Ianieri, CPA	Alan Page, CPA
James Kaiser, CPA	Michael Quinlan, CPA
Paul Kepple, CPA	Michael Swanick, CPA

### Composition

Members of the Board are partners of the firm and are elected for staggered terms of four years that can be renewed once. The Board is chaired by a Lead Director, who is elected by the members of the Board other than the Senior Partner. The Board has at least 12 and not more than 18 members in addition to the firm's Senior Partner.

### Committees

The Board is assisted by various committees that help it to carry out its role. Two committees that assist the Board with its responsibilities related to audit quality are the Accounting & Auditing Practice (A&AP) committee and the Risk Management, Ethics & Compliance (RME&C) committee.

The A&AP committee's scope of responsibility includes regulatory matters that affect our assurance practice and, as appropriate, other parts of the PwC global network, and accountancy licensing and professional standards issues. As part of its oversight of our assurance practice, it evaluates and oversees the progress of our audit quality initiatives, including the status of actions taken in response to PCAOB inspection comments.

The RME&C committee assists the Board in its oversight of the firm's management of key risks as well as the guidelines, policies, and processes for monitoring and mitigating such risks in all practice areas of the firm.

### Board member selection process

The partner vote for selecting Board members is on a headcount basis, where the partners who vote rank the candidates for the Board, and the candidates with the most votes are elected. The Board election is typically supervised by an independent election teller.

[www.pwc.com](http://www.pwc.com)