Governance Insights Center

Overseeing the external auditors

How the audit committee can effectively oversee external auditors during evolving times

August 2026

As a key component of corporate governance, the audit committee serves as an independent and objective body responsible for overseeing the integrity of financial statements and compliance with relevant laws and regulations. Regulators view audit committees as vital gatekeepers that act as a check and balance mechanism to protect investors from potential financial misstatements and fraudulent activities. External auditors play a key role in helping the audit committee discharge this responsibility.

Securities and Exchange Commission (SEC) rules require the audit committee to be directly responsible for appointing, compensating, retaining, and overseeing the work of the external auditors. This makes the relationship between the audit committee and the external auditors important.

Audit committees should look to maximize the value from the external auditor as part of their oversight. In doing so, they should focus on:

- Building a strong working relationship with the external auditor
- Helping protect auditor independence
- Going beyond required auditor communications
- Assessing the performance of the auditor
- Communicating how the committee fulfills its oversight role in proxy statement disclosures

Building a strong working relationship with the external auditor

A strong working relationship between the audit committee chair and the lead audit partner is vital. The strength of this relationship sets the tone for interactions between the committee and the external audit firm.

Creating the right relationship requires continuous communication, open and candid dialogue, and the ability to raise and address sensitive issues. Trust is the foundation. How do you build such a relationship? Here are some leading practices:

- **Be active in selecting the lead audit partner**
  Play a key role in the external audit firm's assignment of the lead audit partner. Consider the individual's skills, experience, schedule capacity, cultural fit, communication style, and other criteria. Being active in the selection process also helps begin the relationship with the lead audit partner right away.
- **Set clear expectations**
  Discuss the audit committee's expectations with the lead audit partner upfront. The discussion can be a valuable opportunity to set the tone, define cadence and the preferred format of communications, and reinforce the need to raise issues in a timely manner.

- **Have regular meetings with the lead audit partner**
  In between audit committee meetings and in preparation for upcoming meetings, the audit committee chair should have informal, one-on-one meetings with the lead audit partner. This promotes candid and timely discussions of issues and concerns and helps develop a strong working relationship.
- **Make the most out of private sessions**
  Many audit committees have periodic private sessions with the external auditors, and some are required to do so. Use this unstructured time effectively to ask candid questions, inquire about sensitive topics, and have confidential conversations.
- **Ask open-ended questions**
  Asking the external auditors open-ended questions can provide an understanding of their perspectives about sensitive and judgmental policies, accounts, and transactions. It can also help prevent overly scripted meetings.
- **Go beyond the lead audit partner**
  It is important to build a relationship with someone at the audit firm other than the lead audit partner—for example, the senior relationship partner or quality review partner. Having another relationship is particularly important when there are service issues or when assigning a new lead audit partner as part of a required rotation.

Helping protect auditor independence

Auditor independence is key—both in fact and appearance. It is key because it fosters high-quality audits, minimizing the possibility that external factors will influence the auditor's judgment, and it promotes investor confidence in public company financial statements. Various SEC and stock exchange listing rules define what auditor independence means.

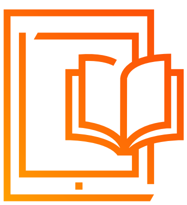
Audit committees are responsible for appointing the external auditors. They play a major role in overseeing their independence.

"Impartiality and objectivity are cornerstones of public accounting, especially in the context of auditing. The profession must fulfill its auditing duties without being unduly influenced by relationships or external pressures. Auditor independence is under increasing pressure in the age of AI due to both technological and ethical complexities."

Source: Kurt Hohl, "**Statement in Connection with the 2025 AICPA Conference on Current SEC and PCAOB Developments**," U.S. Securities and Exchange Commission, December 19, 2025.

Auditor independence should not be just left to the external auditors. Instead, it is a shared responsibility among the audit committee, the auditors, and management. A few key focus areas when overseeing auditor independence include:

- **Audit services**
  Audit committees are required to preapprove all audit services of the external auditor. For audit services, Public Company Accounting Oversight Board (PCAOB) rules require external auditors to affirm their independence in writing. They are also required to disclose to the audit committee all relationships between the audit firm (or any of its affiliates) and the company or persons in financial reporting oversight roles that may reasonably be thought to bear on the auditor's independence. Together, the audit committee, the auditors, and management should have vigorous discussions to determine whether any such relationships could affect the auditor's independence.



- **Non-audit services**
  The audit committee must also preapprove all permitted non-audit services provided by the external auditor. The audit committee should make sure that management and the external auditor have a process for this approval. It should be done prior to engaging the external auditor for the service. The scope of the non-audit services and any potential effects on auditor independence should be discussed with the external auditors and management before preapproving these services. And, if the external auditor is asked to perform tax services or non-audit services related to internal control over financial reporting, the external auditor is required to provide information about the scope, fees, and other details in writing to the audit committee, and to discuss with the audit committee the potential effects of the services on the auditor's independence.

- **Hiring of employees or former employees of the external auditor**
  A cooling-off period is required before a company can hire certain individuals formerly employed by the external audit firm into a financial reporting oversight role. In addition, consideration should be given to whether any former audit professional from the external audit firm continues to have financial relationships with the audit firm (e.g. a pension). By working with management and the external auditor, audit committees can make sure the right process is in place to identify whether any such hiring may impact the external audit firm's independence before hiring decisions are finalized.

- **Impact of significant events**
  Sometimes, certain events at the company can impact external auditor independence. This could include acquisitions, mergers, new board members, or executive management changes. A process should be in place to ensure the external auditor is notified of any such changes well in advance of their occurrence. In the case of a business combination, navigating the independence process could take time, so involving the external auditor early will allow them to evaluate the impact, if any, on auditor independence before the transaction closes. This gives the auditor and management time to evaluate the impact on independence and resolve any issues in a timely manner.

Knowing what SEC-permitted services are allowed

The audit committee has responsibility for preapproving audit and non-audit services provided by the external auditor. But they are limited in what they can approve, since SEC rules prohibit certain services.

What non-audit services are prohibited by the SEC?

- Management functions
- Human resources
- Broker-dealer, investment advisor, or investment banking services
- Legal services
- Expert services unrelated to the audit
- Bookkeeping or other services related to the accounting records or financial statements of the audit client
- Financial information systems design and implementation
- Appraisal or valuation services, fairness opinions, or contribution-in-kind reports
- Actuarial services
- Internal audit outsourcing services

Non-audit fees and proxy advisory firms

Companies are required, in their proxy statement, to disclose fees paid to their external auditor, including those relating to non-audit services. These disclosures can have a real impact on proxy voting. The two main proxy advisory firms, Institutional Shareholder Services and Glass Lewis, both examine this disclosure and use formulas to evaluate whether they consider non-audit fees to be excessive. If so, they may recommend that shareholders vote against ratification of the auditor. Sometimes they also recommend votes against members of the audit committee. These formulas are publicly available on proxy advisors' websites. Furthermore, in efforts to enhance transparency, more companies are disclosing the reasons fees have significantly changed year to year.

Going beyond required auditor communications

Auditors are required to communicate certain matters to the audit committee. And the list of required communications is extensive. However, it is also important for the audit committee to provide the external auditor with its views on risks, fraud, and other matters. These discussions could be mutually beneficial and promote audit quality.

By taking the conversation beyond just what's required, audit committees can enhance their oversight. They can gain deeper insight into the company on a variety of topics, including:

- **Quality of management and corporate culture**
  The external auditor spends a lot of time at the company performing their audit work. They interact with employees and management at all levels. They can share feedback and provide another data point to the board and audit committee on the strength of the finance team, quality of management, tone at the top, and corporate culture.
- **Perspectives on non-financial and financial statement disclosures**
  Depending on where the disclosure is made, the external auditor has either limited or no responsibility over financial information disclosed outside of the audited financial statements. But the audit committee can ask for the external auditor's point of view on these items. This could include information such as non-GAAP measures in an earnings release or disclosures of critical accounting policies and estimates in MD&A in Form 10-K. Non-financial statement disclosures could include ESG metrics and qualitative data within the company's sustainability report, proxy statement, or Form 10-K.

- **Business and industry risks**
  Auditors often have a broad view on emerging trends in the industry. They can also share insights on business risks that the entity may be subject to, based on their work in the industry.
- **Audit committee leading practices**
  The external auditors meet with many audit committees. They can share their views on leading practices other audit committees use to enhance their effectiveness and efficiency, such as agenda planning, pre-meeting preparation, and meeting materials, among others.

Along with these broader discussions, audit committees can expand the dialogue around the external auditor's required communications to gain a better understanding of audit quality, audit efficiency, and the strength of the company's financial reporting. Some topics include:

- Understanding how management plans to adopt new accounting standards or respond to new rules and their level of readiness
- Reviewing the level of coordination between internal audit and the external auditor (e.g. sharing risk assessment information)
- Inquiring about special or new representations in management's representation letter that may highlight higher-risk areas
- Discussing plans for the external auditor to use new and emerging technologies in the audit
- Evaluating the level of audit fees relative to the complexity of operations and efficiencies of IT systems, as well as value and quality of work to be performed and opportunities for efficiency improvements
- Inquiring about findings from statutory audit work performed, including any 'red flags' or themes (e.g. past due reports, qualified audit opinions)

What communications are required?

The external auditors are required to communicate with the audit committee certain things. These topics include:

- **Auditor independence**
- **Audit-related communications, planning**
  - Communications plan
  - Significant issues discussed with management prior to retention
  - Terms of the audit engagement
  - Obtaining information relevant to the audit
  - Overall audit strategy
  - Perspectives on fraud risks
- **Audit-related communications, results of the audit**
  - Fraud
  - Illegal acts
  - Accounting policies and practices, critical accounting estimates, and significant unusual transactions
  - Evaluation of the identification of, accounting for, and disclosure of relationships and transactions with related parties
  - Quality of the company's financial reporting
  - Alternative accounting treatments
  - Changes to the planned audit strategy
  - Identified misstatements
  - Material uncertainties related to events and conditions (specifically going concern)
  - Control deficiencies
  - Other information in documents containing audited financial statements
  - Disagreements with management
- **Other matters**
  - Consultation with other accountants
  - Significant difficulties encountered in performing the audit
  - Other material written communications
  - Fees
  - Difficult or contentious matters
  - The auditor's report, including critical audit matters
  - Auditor quality control procedures
  - Other matters

For additional information on required communications, refer to the **PCAOB's website**.

Critical audit matters

Critical audit matters (CAMs), which are included in a separate section of the auditor's report, are matters that are required or have been communicated to the audit committee, relate to accounts or disclosures that are material to the financial statements, and involve especially challenging, subjective, or complex auditor judgment. Discussions with management and the external auditors are important to understand the types of matters that may be CAMs based on the company's facts and circumstances, the nature of the auditor's planned communications about such matters, and the auditor's response to the CAM. The audit committee may also want to understand the nature of CAMs reported by peer companies' auditors.

Assessing the performance of the auditor

Effective audit committees share their feedback, including issues and opportunities for improvement, with the external auditors. They hold external auditors accountable for action items coming out of the assessment.

Assessing external audit quality is an area audit committees should continuously focus on. Commitment to audit quality begins with an independent audit committee selecting and overseeing the independent auditor and prioritizing quality to encourage auditors to compete based on their ability to perform high-quality audits. The audit committee should regularly assess the auditor's performance to ensure quality.

What should be assessed?

The Center for Audit Quality released a tool to help audit committees with evaluations. The **External Auditor Assessment Tool** provides a general framework and contains sample questions. The sample questions cover:

- Quality of services and sufficiency of resources provided by the external auditor
- Communication and interaction with the auditor
- Auditor's independence, objectivity, and professional skepticism

Another area on which the auditors should be assessed is their continued focus on audit quality. Auditors are turning to technology in order to improve quality and provide audit efficiencies.

Auditor reporting of audit participants

To provide greater transparency into those involved in conducting audits, Public Company Accounting Oversight Board rules require disclosure of the name of the engagement partner. They also require information about certain other accounting firms that took part in the audit including other firms within the same network as the group auditor. The information is filed on PCAOB Form AP: Auditor Reporting of Certain Audit Participants and is searchable on the **PCAOB's website**.

How often should the auditor be assessed and what are possible methods?

Leading practice is to evaluate the external auditor's performance at least annually. Methods for evaluating external auditors vary. Some audit committees use surveys to understand management's views. Others use informal discussions. We recommend that audit committees get management involved. The perspectives of the chief financial officer and chief audit executive can be especially useful. But the key is to focus on what is most important to the audit committee. Audit committee members who serve on other audit committees can also share their experiences working with other external auditors.

Understanding how technology could improve the audit

Auditors are making significant investments in their people and technology to transform the audit experience. Gone are the days of vouching a sample of invoices and tracking the results in an Excel spreadsheet. The audit committee should expect the auditors to have the ability to use AI to perform repetitive activities, extraction technology to pull data, and more.

As a result, new technology enables the auditor to automate the extraction and analysis of data from a company's information systems, eliminating the manual processes of data gathering—a burden on both finance and audit teams.
For more on this topic, **see the appendix.**

The PCAOB's influence

The role of the PCAOB

The PCAOB regulates how external audit firms audit public companies. They set auditing and related professional practice standards that must be followed by registered public company accounting firms as they prepare and issue audit reports. The PCAOB also inspects these firms to make sure they are complying with those standards.

The audit committee should know

- How any new or emerging PCAOB auditing standards could impact the company's audit
- How the PCAOB's annual inspection process of registered public accounting firms could impact the company's audit
- If the audit of the company's financial statements and internal control over financial reporting, if applicable, are selected for a PCAOB inspection, what are the protocols for timely notification to the audit committee, the potential impact on any planned public filings, and the results of the review and any necessary responsive actions
- The audit firm's processes to address prior year PCAOB inspection reports, including whether the audit committee may want to review other audit firms' inspection reports for any lessons learned or similar issues

Audit committees could also review the audit firm's annual quality report as a measure to evaluate the audit firm. Some audit firms release a quality report which includes similar data points to those discussed above and could provide additional insights.

"Everyone who is part of the ecosystem striving to improve audit quality has a significant role to play in achieving our core mission as we evolve to the current and future needs of our capital markets, for the benefit of investors, society, and our world."

Source: Demetrios Logothetis, "**Chairman Logothetis Statement on PCAOB Strategic Priorities**," Public Company Accounting Oversight Board, March 31, 2026.

Communicating how the committee fulfills its oversight role in proxy statement disclosures

Shareholders and proxy advisory firms continue to want to know more about how the audit committee discharges its responsibilities, including its oversight of the external auditors. They consider such information in voting on whether to ratify the appointment of the external auditors as the company's independent registered public accounting firm. And additional disclosure in the proxy statement can help them make that decision.

As a start, audit committees can ask management to benchmark their disclosure. By comparing how their description of oversight of the external auditors compares with that of peer and competitor companies, they might see areas for improvement. The committee can also ask management to draft a sample enhanced disclosure to consider what the committee might include.

A transparent disclosure describing the criteria used by the audit committee in its external auditor evaluation process is becoming more common and expected by investors.

Increase in S&P 500 companies' disclosure around external auditor oversight

Disclosure area	2021	2025	Notes
Audit firm selection/ ratification Disclose considerations in the appointment of company's audit firm	44%	50%	
Audit firm selection/ ratification Disclose the length of audit firm engagement	70%	75%	While there is a requirement for external auditors to include their firm's tenure in the audit report, there has been an upward trend in the number of companies voluntarily disclosing their perspectives regarding their audit firm's tenure
Audit partner selection State that the audit committee is involved in audit partner selection	50%	53%	
Audit firm evaluation/ supervision State that evaluation of the external auditor is at least an annual event	32%	38%	

Source: Center for Audit Quality/Audit Analytics, **2025 Audit Committee Transparency Barometer**, December 2025.

Robust oversight leads to maximized value

Quality financial reporting is critical to the efficiency of the capital markets and protecting investors' interests. The audit committee's role in overseeing the external auditor and the company's financial reporting process are key part of this. Building a strong relationship with the external auditors while keeping an eye on independence and holding them accountable through an annual assessment process will help the audit committee deliver on its oversight role. Transparent disclosure of its efforts and considerations will address the heightened expectations from shareholders, regulators, and other stakeholders. This robust oversight process will ensure that the audit committee gets the most value from its external audits.

Appendix

What audit committees should consider about the external auditor's use of AI in the audit

AI is beginning to change how external audits are planned and performed. Used appropriately, AI and related technologies can help auditors analyze larger volumes of data, identify unusual patterns, focus audit effort on higher-risk areas, and provide deeper insights to management and the audit committee. At the same time, for both issuers and their auditors, AI introduces new questions about reliability, governance, data quality, professional judgment, and regulatory expectations.

For audit committees, the goal is not to become technical AI experts. Rather, the committee should understand where and how the external auditor is using AI, how and whether the auditor is identifying related risks, and that the nature of the auditor's response to the AI-related risks are reflected in the audit plan.

When considering how the auditor is responding to management's adoption of AI and related technologies, the audit committee should expect that AI-related audit responses should be risk-based and tailored to the company's specific facts and circumstances. Companies are adopting AI in different ways and at different levels of maturity. Each company's control environment is different, so the external auditor's approach should reflect an audit response that is reflective of the risks of material misstatement identified in the context of the audit being conducted, including the impact of how AI is used in the company's relevant business processes, internal controls, and financial reporting process, as applicable.

Understanding where AI is used in the audit

The audit committee should understand where AI or AI-enabled tools are being used in the audit and how their use could impact audit quality. This may include areas such as risk assessment, data analysis, anomaly detection, document review, walkthrough support, or audit evidence evaluation and matching. The committee should also understand whether AI is being used to support auditor judgment or whether it is more directly involved in independently producing audit outputs. This distinction matters. AI can be a powerful tool, but it should not replace the auditor's professional skepticism, judgment, or responsibility for the audit opinion.

Understanding how AI tools are governed, tested, and monitored

Audit committees should understand how the external audit firm approves AI tools before they are used on audits. Important areas include how the tools have been developed, deployed, and tested, as well as how they will be monitored over time as they are used. This is especially important because AI tools can produce inaccurate, incomplete, biased, or inconsistent outputs if they are not designed properly and subject to appropriate monitoring. The auditor should be able to explain how the firm evaluates the accuracy and reliability of AI outputs in the context of audit procedures, how it monitors changes in performance over time, and how human review is incorporated.

The external auditor should also be able to describe how AI helps improve audit quality and/or efficiency. As AI technologies are deployed into their audit approach, audit committees should expect a discussion on the auditor's own governance practices, as well as what safeguards are in place to make sure audit technology is used appropriately in combination with human activities.

Understanding the role of people and professional judgment

Audit committees should pay particular attention to the 'human in the loop.' In other words, when AI produces information, recommendations, or exceptions, who maintains responsibility for the outcomes, what information they use, and how that review is evidenced? Human review should be meaningful, not just a rubber stamp. The auditor should be able to explain the qualifications of the people reviewing AI outcomes, when and how issues are escalated, and how the firm addresses the risk that users may become overly reliant on AI over time. This is important because AI may make audit work more efficient, but the external auditor remains responsible for exercising professional judgment and maintaining professional skepticism.

Understanding data quality and security

AI tools depend heavily on the data they use. Poor data can lead to poor outcomes. The audit committee should understand how the external auditor evaluates whether data used in AI-enabled audit procedures is complete, accurate, and appropriate for its intended purpose. Similarly, if the company uses AI in financial reporting, the audit committee should also understand whether sensitive, confidential, or restricted data could be used inappropriately by AI tools. For more on management's use of AI in financial reporting, see the appendix in **Financial reporting oversight**.

Understanding how AI affects the audit plan

As AI becomes more embedded in financial reporting and auditing, audit committees should pay attention to whether AI-related matters are reflected in the management representation letter. For example, management may be asked to make representations about its use of AI in financial reporting, related controls, or the completeness of information provided to the auditor.

The audit committee should also understand how the company's own use of AI affects the external audit plan. If management uses AI in financial reporting, internal controls, forecasting, transaction processing, journal entry review, estimates, or financial statement close processes, the external auditor will likely need to adjust the audit response. Areas of focus could include, among others based on how AI is used and the assessment of risk, whether management has a complete inventory of AI use cases, whether AI tools are subject to appropriate governance, whether data used by AI is complete and accurate, and how controls are adapted to recognize the change in processes when AI is part of the preparation of information or execution of a control. The external auditor should explain how AI-related risks have been considered in the risk assessment, whether any audit procedures have changed, and whether any control deficiencies or observations have been identified.

Understanding regulatory expectations

The audit committee should also understand how emerging regulation, standardsetting, and inspection findings could affect the audit. The committee does not need to track every technical development, but it should understand whether the auditor's AI use aligns with applicable professional standards and regulatory expectations.

Questions the audit committee can ask the external auditor

- How has our company's use of AI affected your audit risk assessment and audit plan? What AI-related risks could affect internal control over financial reporting?
- Where are you using AI or AI-enabled tools in our audit and for what purpose? Are AI tools being used to support auditor judgment, or do they directly produce outputs that affect audit conclusions?
- How do you assess whether the data used by AI-enabled audit tools is complete, accurate, appropriate, and protected?
- How are AI tools approved, tested, and validated before they are used in the audit? What safeguards are in place to confirm that AI outputs are accurate, reliable, and consistent?
- How do you monitor AI tools over time for changes in performance, model drift, or inappropriate outputs?
- How do members of the audit team review AI-generated outputs, and how is professional judgment applied? How are audit team members trained to use AI responsibly and appropriately?
- What third-party AI tools, cloud services, or embedded AI capabilities are used in the audit, and what controls apply to them?
- How does the use of AI improve audit quality, risk assessment, efficiency, or the perspectives provided to management and the audit committee?

For more information

To have a deeper discussion about how this topic might impact your business, please contact your engagement partner or a member of PwC's Governance Insights Center.

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