



I used to work as an auditor and I dreaded major disagreements with company management (which meant more stress, more work, and more scrutiny). Now, as a corporate attorney, I get excited. Here are the basic rules regarding disagreements between public companies and their external auditors:

Taking a step back, the Sarbanes-Oxley Act directs the PCAOB to establish auditing standards for registered public accounting firms to follow in the preparation of audit reports for public companies. So the [PCAOB's Auditing Standards](#) (known as the "AS") is the rulebook for public company audits.

So, what do the AS say about disagreements between companies and their auditors?

AS 1301.22 states in relevant part: "The auditor should communicate to the audit committee any disagreements with management about matters, whether or not satisfactorily resolved, that ... could be significant to the company's financial statements or the auditor's report." Importantly, disagreements with management don't include differences of opinion based on incomplete facts or preliminary information that are later resolved by the auditor after obtaining additional relevant facts or information prior to the issuance of the auditor's report.

In the four years I worked as an auditor, I never saw a disagreement with management make it to the audit committee. Rather, they were kept within the management ranks for several days or weeks while the auditors and management performed additional procedures, reviewed all relevant information and sought resolution of their disagreement. Only if the disagreement persisted at the end of the audit after all efforts were made to resolve it, would it be elevated to the audit committee (assuming it was significant to the financials or audit report).

If a disagreement remains unresolved after escalation to the audit committee, the company or auditor could choose to seek advice directly from the SEC Staff. While the SEC Staff may provide interpretive guidance on issues arising under GAAP or certain securities regulations, they are highly unlikely to referee disputes between companies and auditors - and notably, communications with the SEC may not remain confidential.

Going a step further, the company could decide to fire their auditor, or the auditor could resign. However, and as we'll discuss in a future blog, certain disclosures regarding disagreements with predecessor auditors are required to be made when changing auditors. Additionally, AS 2610.09 requires successor audit firms to ask the predecessor audit firm (prior to accepting the audit engagement) whether they had any disagreements with management as to accounting principles, auditing procedures, or other similarly significant matters.

One last thing to note. While not technically a "disagreement," keep in mind that AS 1301.23 also requires auditors to communicate to the audit committee any significant difficulties (which are broadly defined) encountered during the audit. Thanks to Alea Chatman for her assistance with this one!

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