Shareholder Letters: Accounting Themes

Audit committees and auditors

Berkshire letters: 2002, 1998

Jaeyoon Yu, Ph.D.
Central Michigan University

What the Letter Says

> *“Audit committees can’t audit. … The key job of the audit committee is simply to get the auditors to divulge what they know.”*
>
> Warren E. Buffett, 2002 letter

- Key letters: 2002, 1998
- Course fit: ACC250 — · ACC531 Governance · Difficulty: Intermediate

Step 1: Who Does What

Party	Role
Management	Prepares the financial statements
External auditor	Gives an opinion on them
Audit committee (board)	Appoints and oversees the auditor (SOX 2002)

Step 2: Buffett's Four Questions (1)

1. If the auditor were solely responsible for preparing the statements, would they have been prepared differently from management's way?
2. If the auditor were an investor, would he have received, in plain English, the information essential to understanding the company's performance?

Step 3: Buffett's Four Questions (2)

❸ Is the company following the same internal audit procedure that would be followed if the auditor himself were CEO?

❹ Is the auditor aware of any actions that moved revenues or expenses from one reporting period to another?

- Ask them at least a week before the earnings release.

Back to the Letter

- Buffett (2002): “Audit committees can’t audit.”
- Their key job: get the auditors to **divulge what they know**.
- Buffett (1998): “at times I have been amazed by the numbers that big-name auditors have implicitly blessed.”

Questions

1. Under the Sarbanes-Oxley Act, who appoints and oversees a public company’s external auditor?

   A. The audit committee of the board

   B. The CEO

   C. The CFO

   D. The SEC

2. Buffett suggests the audit committee ask the auditor whether the financial statements would differ if the auditor had prepared them alone. What is the main purpose of such questions?

   A. To prepare the tax return

   B. To make auditors share their concerns about management’s accounting choices

   C. To lower the audit fee

   D. To replace the internal audit function

Sources

- Warren E. Buffett, 2002 letter (berkshirehathaway.com/letters)
- Warren E. Buffett, 1998 letter (berkshirehathaway.com/letters)
- Reading packet and question sheet for this theme

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