

Glass, Lewis & Co., an independent research firm based in San Francisco, has released a comprehensive study of audit fees paid in 2003 and 2002 by more than 2250 public companies in the United States. Glass Lewis' managing director of research, Lynn E. Turner, the former Chief Accountant of the SEC, provides insights and analysis of the data in the report. Among other things, the report reviews fees paid, trends in audit fees and how we recommend investors view audit fees when they vote their proxies. This audit fee study comes on the heels of a widely cited executive compensation report produced by Glass Lewis that reviewed the pay-for-performance record of nearly 1000 public companies.

The audit fee study's key findings include:

- Audit fees at some companies have declined without a reasonable explanation (e.g., **Limited Brands, PG&E, Rite Aid, Monster Worldwide, ImClone Systems, Allergan, Synopsys, Trizec Properties, Wind River Systems, and Rayonier**) or remain relatively low (e.g. **Wal-Mart, Exxon, ChevronTexaco, ConocoPhillips**).
- Overall, fees paid for the audits of financial statements of the Fortune 500 have increased 16% from 2002 to 2003, The increase in fees is not that significant considering during this same time period, the revenues and assets of the Fortune 500 companies surveyed increased 9% and 10%, respectively, and inflation increased 2.3%. (By comparison, companies outside the Fortune 500 saw audit fees increase 22% from 2002 to 2003).
- Fees paid to the auditors for tax work as a percentage of audit fees have decreased from 57% in 2002 to 43% for Fortune 500 companies in 2003. In fact, 126, or over a quarter of those companies paid their auditors less than 10% of their audit fees for tax work in 2003 while 94 had done so in 2002. The numbers were slightly different for companies outside the Fortune 500.
- **Cisco, Ross, Staples, U.S. Bancorp, and Illinois Tool Works** are among 43 companies in the Fortune 500 that paid their auditors tax fees that exceeded the total amount of the fees for performing the audits of their financial statements. In our survey overall, 192 companies of the 2250 paid tax fees that exceeded audit fees.
- Fees paid to auditors for other types of consulting continue to drop with the exception of Deloitte & Touche(DT). In 2003, on average, the Fortune 500 paid consulting fees to their auditors of \$.14 for every dollar paid for audits. This was down from \$.41 in 2002. (Non-Fortune 500 companies, on average, spend significantly more on consulting fees per dollar of audit fees).

- The independence of auditors may be suspect at 20 companies that paid their auditors more for other types of consulting than they did for their audits in 2003. These companies include **Nextel, Nike, McKesson, Walgreen, and Washington Mutual**. This bucks the trend as 1476 companies paid their auditors nothing for other consulting and another 506 companies paid amounts that were less than 10% of the audit fee.
- Companies that disclosed they had retained their auditors to provide services that some believe may impact their independence, such as financial system information design and implementation, appraisal and valuation services, and legal services include **IBM, Altria, AT&T, Ross, Merrill Lynch, Johnson & Johnson, and Nike**.
- The amount paid to auditors for audit-related work such as consulting on internal controls, surprisingly declined from 27% of the audit fees in 2002 to 26% of the audit fees in 2003.
- Some companies within their industry had significantly low audit fees for the size of the company. These included **Sherwin-Williams, Golden West Financial, Winn-Dixie, Owen and Minor, Brinker International, NVR, Progressive, EchoStar, Plains All American, Wal-Mart, Kohls, and Walgreen**. An appendix to the report shows outliers within each industry by audit fees as a percentage of revenue and assets.
- The amounts paid to auditors for the audits of financial statements have increased but not significantly more than the growth in the operations of the companies themselves. The numbers disclosed by companies does not support some of the whining about audit fees discussed in the press.
- For certain services, some auditors have greater levels of conflicts than others, such as PricewaterhouseCoopers (PwC) in tax services and DT in consulting. DT's insistence on retaining its consulting practice has unquestionably led to what investors may well perceive as a greater level of conflict for the companies they audit. Overall, based on the fees paid, KPMG has the lowest level of conflicts.

The full study (in 2 parts totaling more than 125 pages of charts and analysis) is available to Glass Lewis clients at <http://www.proxypaper.com>, under Special Reports (on the left side). Others seeking the full report may contact Glass Lewis at 415-678-4110 or email info@glasslewis.com.