

August 31, 2018

Mr. William D. Duhnke III
Chairman
Public Company Accounting Oversight Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

RE: Strategic Plan 2018-2022

Dear Mr. Duhnke,

We appreciate the opportunity to comment on the Public Company Accounting Oversight Board's (PCAOB's or the Board's) Accounting Standards Board's Strategic Plan (2018-2022) (the Strategic Plan). We laud the PCAOB for its consultative process in developing the Strategic Plan including the survey, direct consultation with key stakeholders and providing for a period of public comment on the Strategic Plan.

CFA Institute,¹ in consultation with its Corporate Disclosure Policy Council ("CDPC")² is providing comments on the Strategic Plan consistent with our objective of promoting fair and transparent global capital markets and advocating for investor protections. An integral part of our efforts toward meeting those goals is ensuring that corporate financial reporting and disclosures – and the related audits – provided to investors and other end users are of high quality.

We have reviewed the five goals of the Strategic Plan of the PCAOB:

- 1) ***Audit Quality*** – Drive improvement in the quality of audit services through a combination of prevention, detection, deterrence and remediation.
- 2) ***Technology*** – Anticipate and respond to the changing environment, including emerging technologies and related risks and opportunities.
- 3) ***Stakeholder Engagement*** – Enhance transparency and accessibility through proactive stakeholder engagement.

¹ With offices in Charlottesville, New York, Hong Kong, London, Mumbai, Beijing and Abu Dhabi, CFA Institute is a global, not-for-profit professional association of more than 133,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 151 countries, of whom more than 125,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 145 member societies in 70 countries and territories.

² The objective of the CDPC is to foster the integrity of financial markets through its efforts to address issues affecting the quality of financial reporting and disclosure worldwide. The CDPC is comprised of investment professionals with extensive expertise and experience in the global capital markets, some of whom are also CFA Institute member volunteers. In this capacity, the CDPC provides the practitioners' perspective in the promotion of high-quality financial reporting and disclosures that meet the needs of investors.

- 4) **Operational Excellence** – Pursue operational excellence through efficient and effective use of our resources, information and technology.
- 5) **Human Capital** – Develop, empower, and reward our people to achieve our shared goals.

Our view is that the Strategic Plan encompasses a broad range of improvements that we support. We have the following observations.

- 1) **Audit Quality** – We note the Board seeks to provide more timely and relevant feedback on its inspection activities. Currently, it remains difficult for investors to gauge improvements in audit quality. We highlight below areas where the Board’s attention to such matters could facilitate improved communication to investors and enhanced credibility for the PCAOB and the audit profession.
 - A. **Inspection Findings** – The current communication regarding inspection findings is challenging for investors to contextualize and incorporate broadly into their investment decision-making process. Investors recognize that audit deficiencies are not necessarily financial reporting errors. We don’t believe inspection findings should move markets or be directly actionable at a company level. That said, investors do need some information on the major issues and trends which provide them with a sense of the quality of the audits which they rely on to protect their interests. Without this, it is challenging to value the audit process.

Citations of large numbers of audit deficiencies or the topical areas where they occur (e.g. fair value) are not particularly helpful. Often the high numbers of audit deficiencies are cited – by the press – but the magnitude of the deficiencies or the implications on the risk of investing are hard to gauge.

Investors seek an understanding of the root causes of audit deficiencies. They seek to understand whether the deficiency drivers are, for example, underlying accounting standard issues, structural audit firm problems, or company process, control or audit committee issues. They seek this understanding to ask better questions or advocate for reforms in a constructive manner.

Better communication on the nature of inspection findings and root causes would improve investor confidence in the quality of audit and the work of audit regulators, including the PCAOB. Swift disciplinary action and communication in the event of high-profile audit failures is also an important deterrent.

- B. **Reconciling Narratives** – Communication from the Board and audit regulators is necessary to counter narratives that diminish investors’ confidence in audit quality and the work of audit regulators.
 1. **Audit Scandals: Fact or Fiction** – Recent publicly reported scandals (e.g. KPMG audit partners, UK audit failures, KPMG South Africa audit issues) and the press associated with them may challenge the narrative of improved audit quality. Recognizing that there is always a disproportionate amount of press attributed to such examples, it would be helpful if the PCAOB and other audit regulators could respond in such situations regarding the steps the regulators take to mitigate and identify more timely such audit failures. For investors in companies listed in the United States, communication regarding how the PCAOB addresses issues at affiliate firms, for example, could improve investor confidence.
 2. **Too Detailed/Not Detailed Enough** – Investors hear from auditors that the PCAOB is too detailed and too focused on immaterial items. On the other hand, when they read about the aforementioned audit scandals it seems the auditors failed to complete basic audit procedures. Investors struggle to reconcile these very different narratives. Communication

regarding how the auditors assess risk and monitor risky clients and how the PCAOB supports them in this endeavor would be helpful in assessing the improvements which are necessary. Recognizing that getting this balance right is always challenging, and that the majority of audits work to mitigate such outcomes, communication by the PCAOB regarding how it addresses such issues would be useful.

Overall, investors are seeking communication from audit regulators that contextualizes other information they receive on audit quality and that communicates actions taken in response to highly visible audit failures to improve future audit quality.

- 2) **Technology** – We strongly support the PCAOB’s inclusion of technology as a separate goal within the Strategic Plan. We recognize the PCAOB’s efforts over the last year to engage stakeholders in a discussion regarding how technology will and should impact the executions of audits.

As an investor organization, we have communicated our concerns regarding the lack of consideration of technology by policymakers in the financial reporting process since, for example, the narrative of disclosure overload permeated the financial reporting landscape in the post financial crisis era.³

As we highlighted in early 2013, in a technology enabled world, the narrative of disclosure overload or the narrative that it is too costly to develop accounting systems in support of accounting standards that improve the capturing, processing, recording and accumulation of transactions into financial statements in a cost-effective manner should be under substantial pressure. For many years, these narratives have been used to stall improvements in accounting and auditing standards. Policymakers must have the requisite understanding of technology in order to evaluate these narratives and should actively question such narratives relative to external evidence that cost-effective technologies are being used to capture, track and process of wide variety of data heretofore not captured.

³ In early 2013, CFA Institute released, [Financial Reporting Disclosures: Investor Perspective on Transparency, Trust and Volume](#). Five years ago, perplexed by a narrative – that included no discussion of technology – that investors were overloaded with disclosures we made the following observations:

Technology: Irreversible Trend Toward Greater Connectivity and Data in Financial Reporting

The majority of accounting standards and financial reporting regulations were written before there was a computer on every desktop (circa 1990) and a smartphone in the palm of everyone’s hand (circa 2010). Prior to the implementation of EDGAR from 1993 to 1996, financial reports of U.S. public companies were not available without a written request to the issuer to mail a copy. EDGAR helped democratize the availability of financial information. Implementation of data tagging using XBRL in 2009–2012 in the United States was an extension of the financial reporting process by allowing data capture at the end of the process, which makes data more flexible and interactive. Similar advancements have been made in jurisdictions outside the United States.

Certainly, significant enhancements have been, or promise to be, made in the delivery of financial reporting information to the investing public. However, when evaluated in the context of the use of technology and the availability of data in other aspects of our lives and in light of the economy, investors see substantial room for innovation and improvement. Consider, for example, the advancement in mapping and direction technology over the same period of time. We have moved from hard copy maps to smartphones that can provide us directions in seconds. Do the reforms in technology related to financial reporting disclosures seem as sweeping? (Page 26)

Consideration for Policymakers to Incorporate in Decisions to Improve Disclosures: Technology

Standard setters and regulators need to look more to the use of technology to facilitate the capture, management, analysis, presentation, and delivery of information to investors. Disclosures broadly, and the disclosure framework specifically, should be developed in the context of advances in technology and connectivity, and they should be responsive to the ever-increasing demand for data. Increased use of technology holds the promise of better (improved quantity and quality of), faster (improved timeliness of), and cheaper (improved access to) information for the user. (Page 93)

In our view, the auditing profession is appropriately responding to the business imperative – and value shifting proposition – brought about by technology enabled processes and is working with the PCAOB regarding how this secular trend should impact the creation of auditing standards and the execution of inspections by the PCAOB. The audit firms, the PCAOB and investors' expectations need to work in lock-step.

Our view is that in the future, investors perception of the greatest value from auditors will be in the areas of greatest judgement and subjectivity (e.g. valuation), not in the auditing of historical transactions that can be automated and validated via technology. Further, technology may change investors perception of the nature of audit risks, how audit evidence can be improved, the use of external data to validate internal company assumptions and judgements, the timing of the execution of audits as well as the manner in which audit results are reported, but this consideration will evolve as the impact of technology is more fully integrated into underlying business and audit processes.

More immediately as it relates to technology, the recent (June 28, 2018) mandate by the SEC of Inline XBRL for all SEC Form 10-Q, 10-K and 20-F filings means that there will shortly be a single, human and machine readable financial statement being produced by companies listed in the United States. Investors can and will increasingly rely on the machine-readable information, but this is currently explicitly excepted from assurance and audit. The PCAOB should examine this anomaly with a view to understanding the problem, ideally with a view to the development of processes and procedures within authoritative literature that can be relied upon by the audit profession. A [2016 CFA Institute survey](#) showed that seventy seven percent of respondents who are aware of XBRL want some level of assurance over the XBRL report — with fifty percent agreeing that the XBRL report should be incorporated into standard financial statement audit. Given the upcoming mandate, this issue is now of even more relevance to investors.

That said, we believe the same degree of engagement and incorporation of technology should be taken into accounting by the FASB in its strategic planning and incorporated into how it creates accounting standards – standards which are used to compile financial statements and against which audits are executed. Accounting, as well as auditing standards, must adapt to a world where investors will pay for – and see value in – standards and audits which provide not only completeness, existence, accuracy, ownership and presentation of historical transactions but on assessment of estimates and valuations included within financial statements. If auditors are simply to provide assurance on highly automated historical transactions – much of what comprises today's accounting standards – the auditing profession's value will decrease to investors.

In our view, the FASB should become engaged with the PCAOB in the consideration of the audit of highly technologically enabled transactions and to incorporate these perspectives into the accounting standard-setting upon which auditing standards are applied. We believe the PCAOB should include the FASB in its technology task force such that the accounting standard-setters benefit from these useful conversations.

Overall, the PCAOB's articulation of technology as a strategic objective is important and we believe other policymakers should take note.

- 3) **Operating Plans** – Because of the significant turnover at the Board this year, we believe it is important for the Board to communicate in more detail about its operating plans such that stakeholders have an understanding regarding how these strategic goals are going to be achieved.
- A. **Research & Standard-Setting Agendas** – Investors – as well as other stakeholders – are interested in changes in the PCAOB’s standard-setting and research agendas as the long-term nature of such projects provides insight into the direction of the Board and the organization more broadly. As it relates to the research agenda, investors are keenly interested in work related to alternative performance measures (e.g. Non-GAAP measures and other metrics) as well as on emerging forms or reporting (e.g. ESG, sustainability). These are areas where investors are continuing to see a burgeoning number of metrics and disclosures without a great deal of comfort on the quality of such information. As we note above, assurance over XBRL information is another area of interest to investors. As we always look to improve the strength of and communication from audit committees that are appointed by investors to protect their interests.
- We note in the Strategic Plan your acknowledgement of the need to cooperate more extensively with international standard setters and regulators. This is one area where such cooperation could benefit investors who have limited resources to address similar issues at different times with slightly different outcomes.
- B. **Economic Analysis** – Similarly, investors are keen to understand how the new Board will execute its cost vs. benefit analysis. Because investors – those who ultimately bear the cost of new accounting and auditing standards – routinely hear that new standards are too expensive to implement, we are keen to understand how the Board will weigh the direct costs, which are often overstated, and the benefits, which are less measurable, but derived most substantially by investors. We highlight the economic analysis because it provides an opportunity to gauge the degree to which the Board stands in the shoes of investors in making their cost/benefit trade-offs.
- C. **Post Implementation Reviews** – The PCAOB has issued several new standards over the last few years – most specifically related to its transparency projects. We believe it will be important to do post implementation reviews of such standards. We recognize the most subjective of these changes is the implementation of the disclosure of critical audit matters (CAMs), which will first be implemented for year-end 2019. We believe it is important for the PCAOB to do a post implementation review of the adoption of this standard and release the results publicly. This element of the new auditor’s report, is the audit standard with the most visible impact to investors. As such, investors will be interested to learn whether the implementation meets the PCAOB’s expectation. For most auditing standards, investors do not have direct line of sight into the output or results of a standard. CAMs are different and allow the PCAOB to illustrate its commitment to improving communication between auditors and their clients (i.e. investors).
- D. **Process Improvements** – In numerous places throughout the Strategic Plan there is mention of improving processes, leveraging technology to improve processes, and use of data in enabling decision-making. It may be helpful to provide clarity on the nature of the processes under review and the investment – in both time, timing and money – to effectuate such change.

Direct communication regarding personnel appointments – as we discuss below – as well as the standard-setting agenda and research agendas, economic analysis and process improvements are particularly important such that stakeholders are not left inferring the direction of the PCAOB.

- 4) ***Stakeholder Engagement*** – We have always found the PCAOB effective at engaging with a variety of stakeholders as it pursues its standard-setting agenda, for example. We encourage the Board and staff to engage through not only advisory committees but also conduct direct outreach to stakeholders. Each serves a different purpose. We agree with a review of the various advisory committees and with the objective of making them more interactive, but we would strongly oppose an elimination of either. There is an unquantifiable benefit to having discussion of issues in an open setting with a variety of stakeholders. It affords an exchange of ideas on both a formal and informal basis and the ability to learn and appreciate the perspectives other stakeholders. We recognize the effort by PCAOB staff that goes into each of these meetings and we believe they are worthwhile endeavors.
- 5) ***Personnel*** – Substantial turnover in the last six months at the PCAOB has left several key positions filled with interim personnel. The individuals filling these positions will provide insight to investors and others regarding how the PCAOB seeks to execute its goals and underlying objectives. We don't disagree with any of the strategic objectives, but we believe how these positions will be filled will send a strong message regarding the PCAOB's strategic direction over the next decade. Investors watch with interest to determine if such individuals have the requisite technical expertise in auditing and whether they come equipped with an investor mindset that recognizes audit clients are investors – not the management of the company under audit. Such individuals will also set the tone for creating dialogue with stakeholders.
- 6) ***Communication Regarding Progress Against Strategic Goals*** – Finally, we believe it would be useful for the PCAOB to provide an update on the progress on their Strategic Plan in the next several years as some of the initiatives are implemented.

If you or your staff have questions or seek further elaboration of our views, please contact Sandy Peters by phone at +1.212.754.8350 or by email at sandra.peters@cfainstitute.org.

Sincerely,

/s/ *Sandra J. Peters*

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