

Via E-Mail

January 24, 2022

Erica Williams
Chair
Public Company Accounting Oversight Board
100 F Street NE
Washington, DC 20549

Dear Chair Williams and Board Members DesParte, Ho, Stein, and Thompson:

The CFA Institute¹ congratulates you on your appointment to the Public Company Accounting Oversight Board (“PCAOB” or “Board”). CFA Institute has a long history of promoting fair and transparent global capital markets and advocating for strong investor protections. An integral part of our efforts toward meeting those goals is ensuring that corporate financial reporting and disclosures – and the related independent audits – provided to investors and other end users are reliable and of high quality.

The Objective of Our Letter

As you begin your tenure, we look forward to working with you and your senior staff to advance transparency and accountability in the U.S. capital markets. Our letter is primarily focused on matters related to the Board’s authority and responsibility for overseeing the auditors of public companies, protecting the interests of investors, and furthering the public interest in the preparation of informative, accurate, and independent audit reports.

We would welcome the opportunity to meet with each of you for a conversation about our mutual interest in strengthening the U.S. capital markets. We provide this letter as background to such a meeting.

Increasing the Effectiveness of the PCAOB and High-Quality Audits

Financial reporting standards facilitate the preparation and dissemination of consistent, comparable, decision-useful information to investors, other stakeholders and others. In order for investors to have confidence in the representational faithfulness of the information, however, it must be subject to a rigorous independent audit.

Overarching Considerations

CFA Institute has long advocated for audit reforms globally. We have advocated for audits of internal controls and auditor oversight reforms brought about by legislation such as the U.S. Sarbanes-Oxley Act of 2002 (“SOX Act”) and similar regulation globally. CFA Institute has been one of the most thoughtful, technically competent, and consistent commentators on topics related to audit quality from the perspective of investors during the PCAOB’s existence. We have participated in PCAOB advisory committees, met with board members and staff, provided comment letter responses to PCAOB consultations, and

¹ With offices in Charlottesville, New York, Washington, DC, Brussels, Hong Kong, Mumbai, Beijing, Shanghai, Abu Dhabi and London, CFA Institute is a global, not-for-profit professional association of more than 181,000 members, as well as 160 member societies around the world. Members include investment analysts, advisers, portfolio managers, and other investment professionals. CFA Institute administers the Chartered Financial Analyst® (CFA®) Program.

conducted surveys and outreach to our investor members to inform the investor views we bring to the audit regulator and the audit profession. Such outreach has included not only work related to SOX, but also reforms to enhance the auditor's report and to increase transparency regarding audit participants (e.g., disclosure of engagement partner names, auditor tenure and use of affiliated firms).

Our organization performs a vital function of translating auditing standards and regulation – and their effects – to the investor community as well as bringing investor views to the PCAOB. Investors speak the language of investing, while accountants speak the language of accounting. More challenging for investors is that auditors – and audit regulators – speak still another language – the language of auditing. Because of the lack of transparency regarding audits, investor input on auditing issue is even more challenging.

As the new PCAOB members embark on their work, we believe there are three particularly important considerations to guide your thinking and efforts:

- (1) *Audit is a Credence Good: Transparency From Those Charged with Protecting, and Compensated By, Investors Must Be a PCAOB Priority*** – Audits are a [credence good](#)² whereby the quality of the audit is difficult for the purchaser – the investor – to assess even after purchase. For that reason, in our recent work related to audit reforms in the United Kingdom³ we have focused on enhancing transparency, oversight and accountability of those hired (e.g., management, the audit committee, auditors and audit regulators) to protect the interests of investors. We encourage the new PCAOB members to review our UK audit reform consultation responses (i.e., see footnote 3) because they provide an excellent compendium of our views on audit, audit competition, audit quality and auditor supervision and oversight. Specifically, we would point you to Appendix A to [our Brydon comment letter response](#) as it includes a comprehensive list of our work related to audit.

² Colleen Honigsberg, Phd, Professor of Accounting at Stanford Law School [rightly highlighted this point](#) at a [September 9, 2021 meeting of the SEC Investor Advisory Committee](#). It is a sentiment we expressed in our letter to the UK Government during its recent audit reform efforts.

³ CFA Institute has responded to the UK Government's efforts regarding improving the audit regulator ([Kingman Review](#)), competition in the audit market ([CMA Review](#)) and audit quality ([Brydon Review](#)) in 2018 and 2019 as well as the 2021 UK Government's Department of Business, Energy & Industrial Strategy (BEIS) overarching consultation (BEIS Overall Consultation), [Restoring Trust in Audit and Corporate Governance: Consultation on the Government's Proposals](#). In 2019, CFA Institute provided comprehensive responses to [Sir Donald Brydon's Independent Review of the Quality and Effectiveness of Audit](#) and the [Competition and Market Authority \(CMA\)'s Statutory Audit Services Market Study](#) proposals. Jointly with the Council of Institutional Investors (CII), we also provided in 2020 [our views to BEIS on the importance of internal controls over financial reporting](#). In 2021, we provided a [response](#) to the [BEIS Overall Consultation](#).

As the largest global organization of professional investors who have advocated for meaningful audit reforms globally, we devoted significant time to our consideration of UK government audit reform initiatives because:

- a) audit reforms in the UK will have an impact on other audit markets given the global nature of the listed public companies subject to audit and the interconnected and global nature of the largest accounting firms;
- b) the UK audit profession has both a legacy and contemporary impact on the audit profession – a profession meant to serve the interests of investors and the public interest; and
- c) we do not see the foundational elements of high-quality audits as being jurisdictionally specific⁴ - rather, the elements of high-quality audits are global.

For these reasons, we believe these UK audit reform responses are relevant to the PCAOB in the context of the US audit market. They are also why we highlight our PCAOB consultation responses to regulators and legislators in other jurisdictions.

You will note our request, throughout all of the aforementioned consultation responses, for greater transparency by those meant to serve investor interests. We view transparency to investors as an overarching consideration for PCAOB Board members as they engage in their work. ***It is also important to remember that investors – as the residual owners of the public company under audit – compensate not only management, the audit committee, and the auditors but also – through assessments of US public companies – the PCAOB. Through the mission and the compensation of the PCAOB, investor primacy – including transparency and communication to investors – should be a guiding principle for the new PCAOB.***

- (2) ***Investor Outreach Must Be Effects, Not Audit Language Focused*** – Because investors and auditor speak different languages and the investor (consumer of audit services) gets little insight into the quality of the good, when developing or creating new auditing standards ***the audit regulator must conduct outreach that explains the nature of the change being proposed and its effects on investors in a language other than auditing ease.*** Without such translation, the input the PCAOB will receive will not be as useful as it otherwise could be. Investors are smart. They are not confused (i.e., a common refrain used by other stakeholders to forgo change) by accounting and audit standards when they are communicated in terms of their effects on the audit, the accounting, and the economics of the companies in which they invest. It is always important to remember that investors – not management, the audit committee, the auditors, or the audit regulators – are the one's putting money at risk. Investors simply need the jargon of the audit profession to be translated into the effects on auditors, audits and financial statements. With that translation, you will find investors are able to provide rich and useful feedback to the PCAOB.
- (3) ***Audit Quality Indicators: A Focus for the PCAOB*** – We would also highlight the importance of audit quality indicators (AQIs) – a standard-setting agenda item we highlight below – to investors. The project on audit quality indicators has been repeatedly delayed. There is a perception – almost mystique – that audit quality is an elusive, unmeasurable quality. We disagree. There are many products (i.e., products that are much more vital to our lives) where measures of quality are routinely defined, measured, and monitored – and adjusted over time – at the specific product level. Audit is no different. While firm level information, quality standards and transparency reports are important,

⁴ CFA Institute will be providing a response to the European Commission's, [Consultation Document Strengthening Of The Quality Of Corporate Reporting And Its Enforcement](#), which seeks comment on items such as reforms related to auditors and the regulators who supervise them. There we will provide our views on high-quality reporting and audits in the context of the European Commission's framework.

they are not sufficient. Engagement level audit quality indicators provide management, the audit committee, the audit regulator, and the consumer (investor) with metrics to communicate and measure progress. Measuring audit quality is about providing more information to investors – and the agents engaged to protect their interests – to move audits out of the realm of a credence good. What gets measured gets monitored. The delay in developing audit quality indicators is, in the view of some, and indicator of their potential to be highly effective.

Without the transparency that can be achieved through audit quality indicators there cannot be trust and without trust there cannot be confidence by investors in the audit profession. As investors we respect and want to work with the audit profession – as we, not the audit committee or management, are their client. We have a mutual interest in seeing the audit profession succeed and we do not believe the audit profession – because of a lack of transparency – should be judged by their worst moments – as reported in the press upon high-profile audit failures – but by the good work members of the audit profession undertake each day.

PCAOB Priorities

We respectfully submit our views on certain items or priorities that we believe result in an effective PCAOB:

- (1) *Conduct a Strategic Review*** – In August 2018, the PCAOB published a draft [Strategic Plan \(2018-2022\) with a request for public comment](#). The PCAOB received [thirty-three comment letters](#) in response to its request, including [one from CFA Institute](#). Since 2018, the PCAOB Board has reaffirmed its 2018 plan with little change. ***We have seen little progress on the Strategic Plan in the three years since its issuance.***

Further, some have expressed concern that the PCAOB, once a leader in audit oversight, has demurred, becoming a laggard. ***In numerous instances the PCAOB – despite having more independent funding – has allowed the International Auditing and Assurance Standards Board (“IAASB”) to lead the way on standard-setting seeking to mimic or mirror their work. As investor advocates, we have found international and European audit regulators, at times, to be more progressive and responsive to investor needs and strategic priorities.*** We urge the new Board to re-evaluate its agenda and seek public comment on whether it should be a leader or follower in global reforms of audit oversight.

The beginning of a new Board presents a timely opportunity for the PCAOB to reexamine its priorities with the benefit of public input. For that reason, we believe the newly constituted PCAOB should seek public input on strategic priorities and direction.

- (2) *Create an Active, Public and Investor Centered Agenda*** – The PCAOB should revise its standard-setting and research agendas to reflect the interests of investors in furthering audit quality.

The PCAOB ceased publicly exposing and discussing its research and standard-setting priorities with the public and investors in 2018.⁵ In September 2020, the PCAOB updated its [standard-setting](#)

⁵ Prior to 2018, most, if not all, of the PCAOB's published standard-setting and research agenda items, for over a decade, were routinely discussed with the PCAOB's Advisory Groups. In its periodic standard-setting and research agenda updates, the PCAOB staff noted that the "standard-setting agenda is informed by the PCAOB's oversight activities, monitoring of the environment, consultation with the PCAOB Board's Standing Advisory Group ("SAG"), input from the PCAOB Board's Investor Advisory Group ("IAG"), discussion with the U.S. Securities and Exchange Commission ("SEC") staff, and other factors." See PCAOB, OCA, Standard-Setting

and research priorities. *The update removed items⁶ that investors had repeatedly identified as important*, including:

- An Auditor's Role Regarding Other Information and Company Performance Measures, Including Non-GAAP Measures;
- An Auditor's Consideration of Noncompliance with Laws and Regulations (NOCLAR); and
- An Auditor's Consideration of an Entity's Ability to Continue as a Going Concern.

Moreover, the listed priorities fail to consider the need to modernize existing “interim” standards that were developed well in advance of the establishment of the PCAOB in 2003. *The revised priorities reflect deference⁷ to the projects of the IAASB*. Former PCAOB Board Member J. Robert Brown called this change a “tragic mistake” and criticized the PCAOB Board’s focus on deference to international audit standard setters.

We also note that the PCAOB – some suggest because of lack of staffing priority at the Office of Chief Auditor – has had no additional standard-setting projects over the last four years.

We have given consideration and thought to an investor-centric agenda, and we would welcome an opportunity to discuss this with you. We note the following as elements of such an agenda.

A. Modernize Interim Auditing, Attestation, Quality Control, Ethics and Independence Standards

- i. The PCAOB adopted the compendium of the profession’s legacy auditing, attestation, quality control, and ethics standards (i.e., AICPA standards) in 2003. The PCAOB has not updated many of the legacy, and the latest standard-setting agenda does not indicate the timing or whether there will be any future consideration of whether the legacy standards in effect remain fit-for-purpose. The PCAOB should prioritize a [project](#), with public input, on whether the standards remain fit-for-purpose and the nature and extent of whether any modernization is necessary.
- ii. The PCAOB should continue to advance its project to improve the standards relating to an audit firm’s system of [quality control](#) including provisions, such as structural mechanisms to promote [independent oversight of a firm’s system of quality control and the mitigation of commercial interests over maintaining audit quality](#). (See also [PCAOB Rulemaking Docket 046: Quality Control](#)).

Agendas, Oct. 14 -15, 2009; Oct. 2010; Sept. 30, 2011; Mar. 2012; Nov. 2012; Mar. 31, 2013; Dec. 10, 2013; Dec. 31, 2013; Mar. 31, 2014; June 30, 2014; Sept. 30, 2014; Dec. 31, 2014; Mar. 31, 2015; Sept. 30, 2015; Dec. 31, 2015; Mar. 31, 2016; June 30, 2016; Sept. 30, 2016; Dec. 31, 2016; Mar. 31, 2017; June 30, 2017; Dec. 30, 2017; Mar. 31, 2018; and June 30, 2018. The PCAOB staff did not issue standard-setting updates subsequent to June 20, 2018.

⁶ The PCAOB staff explained: "We have removed Going Concern from the standard-setting agenda and Other Information and Noncompliance with Laws and Regulation from the research agenda. Following significant work on these projects, we have concluded there is not a need at present to change our standards or take other action on these topics."

⁷ See Mark Maurer, [How International Auditing Rules Are Shaping Standards in the U.S.](#), Wall St. Journal. (Jan. 20, 2020).

- B. Propose Audit Quality Indicators (AQIs)** – In 2012, the PCAOB began a project to develop and track audit quality measures “with respect to domestic global network firms and reporting collective measures over time.”⁸ In 2015, the PCAOB issued a [Concept Release](#) but little further progress has been made. The PCAOB’s Office of Economic and Risk Analysis has been studying the issue of possible quantitative measures of audit quality. Both [CFA Institute](#) and the [Council of Institutional Investors](#) have indicated support for promulgation of quantitative measures of audit quality and suggested that such measures be included in a future PCAOB standard to modernize the standards concerning an audit firm’s system of quality control.
- C. Modernize the Auditing Standards to Address the Increased Use of Technology in Conducting the Audit**
- i. Over the last number of years, use of automated tools, machine learning, and artificial intelligence has greatly impacted the risk assessment and nature, timing, and extent of auditing procedures. This revolution or wave of digital auditing has occurred without appropriate consideration of the impact on audit quality. The PCAOB notes that its standards “do not explicitly encourage the use of such tools or indicate when their use might be appropriate or highlight risks or pitfalls.”
 - ii. Moreover, the PCAOB has not addressed the SEC’s mandated incorporation of XBRL into the filed financial reports (termed [Inline XBRL](#)). All large and accelerated filers must file using Inline XBRL in 2021. There are no standards, however, to ensure that XBRL data is reliable or consistent with the visual document. The PCAOB should consider guidance or other authoritative literature to address gaps in the standards that fail to address the use of technology in the financial reporting process.
 - iii. The PCAOB’s project on [audit evidence](#) is greatly impacted by the emerging technologies used in business processes and in public company auditing.
- D. Modernize the Auditing Standards to Address the Distributed Nature of Auditing Procedures** – The nature of audits of increasingly global companies and the continued use of remote audit techniques results in a greater proportion of audit work being conducted by “[other auditors](#)” or service centers creating challenges in coordination and communication. The COVID-19 pandemic has also required changes to the nature, timing, and extent of audit procedures, including the dominance of “remote” auditing. The PCAOB should continue to advance its project on the supervision of the work of other auditors, including the consideration of appropriate oversight of service centers. We note the PCAOB issued a second supplemental request for comment on this topic in late 2021. CFA Institute [filed a comment letter response](#) on this consultation.
- E. Establish and Promulgate Rules for a Whistleblower Program** – The PCAOB hosts a “Tip & Referral Center” but does not have a comprehensive program to protect or incentivize whistleblowers. In 2019, the U.S. House of Representatives passed the PCAOB Whistleblower Protection Act. The bill was not passed by the Senate, and accordingly, did not become law. The PCAOB should consider whether it has the authority to provide for a whistleblower program without Congressional intervention.

⁸ Public Company Accounting Oversight Board Strategic Plan, 2012-2016, November 20, 2012, p.5.

- (3) **Advisory Groups: Excluding Investor Organizations** – In 2018, the PCAOB Board effectively disbanded its two advisory groups⁹ after adopting its [2018-2022 strategic plan](#).¹⁰ We have expressed concerns to the PCAOB Board members about its failure to convene advisory groups for the last 3 years (the last meeting was in November 2018).

In early 2021, the PCAOB adopted changes to its advisory groups that have the effect of excluding investor input. ***The PCAOB, formed a new advisory group, and, without prior public notice, dissolved its two advisory groups. The PCAOB took such action in a matter of days and after the departure of the sole member representing investor views.***

Despite the lauding of investor engagement in the press release and board member statements, its new advisory group’s charter, substantively excludes participation by investor groups, such as CFA Institute. The PCAOB’s action relative to investors is inconsistent with the treatment of the auditing profession which would select and nominate members to PCAOB advisory committees.¹¹

The new charter calls for involvement only by investors engaged directly in the investment decision-making process. Participation in the advisory committee by preparers, audit committee members and the audit profession – on the other hand – may be by individuals not directly involved in the preparation or audit of company financial statements, not audit committee members or not directly engaged in auditing financial statements (i.e., positions on such committees from the Big 4 are filled by individuals in national offices who are not directly executing audits). Investors have limited insight into the audit with, until recently, only a boiler-plate binary audit opinion. Investors are the risk bearing party in this advisory committee dialogue, but will be placed in the position of having the least knowledge of the audit standards and the auditor work product – as they have no transparency into this audit process, as we describe above.

As we noted previously, organizations such as CFA Institute and the Council of Institutional Investors have served an essential function for the investment community in translating the audit standards to the impacts they will have on investors’ interests and investment decision-making. We have responded to comment letters – and engaged more substantially in the development of auditing standards – more than any other investor organizations over the last decade – using our investor outreach capabilities to obtain input that bridges the language of auditors and accountants to that of

⁹ The PCAOB established its Investor Advisory Group (IAG) in July 2009 as a “forum for those representing investors to provide...views and advise on matters affecting investors and the work of the PCAOB.” The PCAOB established its Standing Advisory Group in June 2004 “to provide expert advice and recommendations...”

¹⁰ As noted in the [PCAOB Strategic Plan 2018-2022](#) (November 15, 2018): “Numerous commenters addressed our advisory groups, with some supporting a continuation of the existing advisory groups and others supporting significant changes to them. As we reassess our use of advisory groups in connection with Goal 3, Objective 2, we will carefully consider the positions set forth in the comment letters. We expect to announce changes to our advisory groups shortly.”

¹¹ ***The PCAOB’s advisory group charter may violate its own bylaws.*** PCAOB Rule 3700(c) provides that “members of advisory groups will be selected by the Board, in its sole discretion, based on nominations, including self-nominations received from any person or organization.” However, the PCAOB Board’s newly adopted charter stated that it would select audit professionals “based on nominations from the Center for Quality...” The PCAOB Board stated that the Center for Audit Quality is “an organization that represents the public company audit profession and...is affiliated with the American Institute of CPAs (AICPA)”.

investors. Exclusion from advisory group participation has the impact of disenfranchising investors and begs the question: *Is input by investor organizations to consultations considered investor input?*

At that time – and for the reasons noted above – we requested that the SEC encourage the PCAOB Board to reverse this precedent-setting action.

As a former a member of the PCAOB’s Standing Advisory Group (now dissolved), the public forum served several important functions as follows:

- It allowed stakeholders to make positions (other than expressed in comment letters) and conversations public;
- It enabled stakeholders to publicly engage and exchange ideas rather than having conversations directly with the PCAOB – thereby creating a public, interactive exchange of ideas and views; and
- It allowed the public to witness the meetings and the press to communicate the exchange to a broader audience.

We have witnessed in these public meetings that public statements can bring about consensus and change the direction of projects – for example, as it did with the disclosure of audit partner names when company CFOs publicly expressed that if they are named, so too should audit partners be disclosed.

We note that, in the Spring of 2021, the Board sought candidates for the new Standards Advisory Group, despite our request to reverse course. Those submissions were deferred, however, upon the SEC decision to reconstitute the PCAOB. We believe addressing the status of the advisory committees promptly is an important demonstration to the public, especially investors, of the PCAOB’s commitment and forward direction.

(4) *Transparency and Accountability* – The PCAOB should adopt [rules](#) to enhance its [transparency and accountability](#) for the benefit of investors.

- *Public Meetings* – The PCAOB’s Chairman can elect to hold meetings publicly or behind closed doors with the exception that current rules require one public meeting each calendar quarter. ***The PCAOB under the prior leadership, however, did not uphold this rule.¹² This approach should be rectified under the current administration.***

Further, the PCAOB should amend its rules to adopt similar measures of transparency required of government agencies, including provisions for holding open meetings, publishing the timing of closed meetings (and the nature of any exemption from holding an open meeting), and disclosing member votes.

- *Public Notice & Consultation* – The PCAOB also recently adopted changes to its [independence standards](#) without prior notice or exposure to stakeholders or the public. **The PCAOB should**

¹² During 2020, the PCAOB did not adhere to this rule. As per the [PCAOB website](#), the PCAOB held only one public open meeting in 2020, two in 2019, and two in 2018. The PCAOB bylaws ([Article 5.1](#)) require a minimum of four per year. Prior to the change in administration and SEC leadership – and expression public concerns – there was only one board meeting in 2021 to make the changes related to the advisory groups as noted elsewhere herein.

amend its rules to require notice and comment prior to rulemaking/standard setting to provide for public notice, consideration, and comment.

- *Meetings with Regulated Entities* – The PCAOB members and staff meet with regulated entities (e.g., the audit firms it oversees) without transparency. This could undermine the perception of the PCAOB’s independence from the audit profession. The PCAOB should provide public disclosure of meetings with stakeholders, particularly with regulated entities.
- *Chair Calendar* – The PCAOB Chair should publicly disclose a calendar (similar to the one [published by the SEC Chair](#)) detailing activities and meetings with staff and other PCAOB Board members.

Thank you for your consideration of our views and perspectives. Again, we would welcome the opportunity to meet with you to provide more detail on our letter. We also look forward to collaboration throughout your tenure. If you have any questions or seek further elaboration of our views, please contact me by email at sandra.peters@cfainstitute.org or by phone at 347.413.0774.

Sincerely,

/s/ Sandra J. Peters

Sandra J. Peters, CPA, CFA
Senior Head, Global Financial Reporting Policy Advocacy
CFA Institute

CC: Chair Gary Gensler
Commissioner Hester Peirce
Commissioner Allison Heron Lee
Commissioner Caroline Crenshaw
Acting Chief Accountant Paul Munter