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Ms. Phoebe W. Brown, Secretary
Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

10 September 2018

Re: Strategic Plan 2018-2022 – Draft for Comment

Dear Ms. Brown:

Ernst & Young LLP (EY) is pleased to submit these comments to the Public Company Accounting Oversight Board (PCAOB or Board) on its draft Strategic Plan 2018-2022 (Draft Plan). We appreciate this opportunity to comment and commend the PCAOB for seeking input from a wide array of financial reporting stakeholders.

We believe the PCAOB has been effective in its mission as an independent audit regulator, furthering audit quality and protecting investors. We agree with the view expressed in the Draft Plan that audit quality has improved substantially under the oversight of the PCAOB. Since its creation by the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley), the PCAOB has led a transformation in audit oversight, laying a strong foundation upon which many other regulators around the world have built.

We believe the independent audit is fundamental to the quality of corporate financial reports and investors' trust and confidence in them. Provisions of Sarbanes-Oxley, including the PCAOB's creation, the enhancement of the audit committee's role and audits of internal control over financial reporting, have collectively contributed to improvements in the quality of financial reporting and the independent audit. In 2017, the level of corporate financial restatements was at its lowest point in close to two decades.¹ The severity of restatements also is at a historically low level. Investors have high levels of confidence in audited financial statements and auditors, as demonstrated by recent surveys.² PCAOB inspection findings, while only one factor in the overall assessment of an audit firm, also continue to improve. Over this time, EY, like its peers, has made significant investments to enhance the skills of its professionals and our system of quality control, as well as develop technology and other tools to advance audit quality.

¹ Don Whalen, Olga Usvyatsky and Dennis Tanona, "2017 Financial Restatements - A Seventeen Year Comparison," Audit Analytics, June 2018.

² "Main Street Investor Survey," Center for Audit Quality, 25 October 2017, thecaq.org/2017-main-street-investor-survey, accessed August 2018.

An effective audit regulator is also a critical driver of audit quality. One example of how the PCAOB has improved audit quality is through its remediation framework, the process it uses to evaluate a firm's activities to address quality control findings identified in inspections. This framework encourages audit firms to examine their understanding of the root causes of the identified quality control concerns. Confronting root causes allows firms to design and execute more effective remediation activities, which can result in more timely improvements in audit quality.

While it is important to recognize the progress made since 2002 in advancing audit quality, we agree with the PCAOB that more must be done. EY takes our responsibility for performing quality audits and our commitment to investors very seriously. We will continue to engage with the PCAOB to provide our insights on the audit and how audit oversight and audit standards can continue to evolve.

General views on the Draft Plan

We commend the Board's forward-looking approach in the Draft Plan as we all grapple with the fast-moving business environment and technological disruption. Adjusting to the dynamic environment is critical for the PCAOB, the profession and all of the PCAOB's stakeholders. The pace and nature of change and auditors' increasing ability to review and utilize significant amounts of data present new risks as well as tremendous opportunities to enhance the value of the audit to investors and others.

The PCAOB's Draft Plan outlines important and sensible goals and objectives that we believe will focus PCAOB actions on promoting higher levels of audit quality and protecting investors in today's fluid environment. The plan identifies several important risks to audit oversight and also recognizes the extensive opportunities for the PCAOB and its various stakeholders – including firms, audit committees, preparers, investors and academics – to work together to advance audit quality and investor protection.

We have identified certain areas of the Draft Plan that we believe merit further discussion, given their importance to audit quality and effective oversight. Below, we provide some additional comments and suggestions for the Board's consideration in three areas: evolution of PCAOB reporting to drive audit quality improvements; meeting the challenge of the evolving technological landscape; and stakeholder engagement and communication. We also refer the Board to the comment letter on the Draft Plan from the Center for Audit Quality (CAQ), which identifies additional areas for consideration. We look forward to engaging with the PCAOB along with other stakeholders to advance the implementation of the Strategic Plan.

Evolution of PCAOB reporting to drive audit quality improvements

We welcome the PCAOB's objective of reporting on inspection activities to "provide more timely and relevant feedback,"³ as we believe the PCAOB has the opportunity to advance audit quality through its publicly issued reports on inspection findings. We agree that enhanced reporting could help firms prevent and remediate deficiencies. We believe it also should give other consumers of the reports information that can be more readily understood and used. Today, most of what is reported is

³ Draft Strategic Plan, p. 7.

inspection deficiencies. The reports do not address the severity of the deficiencies, which gives an incomplete picture of audit quality, especially for those not directly connected to the profession or steeped in the nature of audits.

As the PCAOB moves to implement this objective and make reports more informative, we believe the PCAOB should:

- ▶ Define the PCAOB's objectives of inspection reporting – both at an individual firm and a collective (multi-firm) level – as well as modify how the PCAOB reports information to the market and clarify how stakeholders might want to use those reports
- ▶ Identify and promote leading practices for audit firms through expanded collective public reporting of audit quality trends based on PCAOB inspections, including through 4010 reports⁴
- ▶ Identify trends in inspection findings
- ▶ Differentiate between findings based on the severity of a finding
- ▶ Provide more timely inspection feedback to audit firms so issues can be addressed quickly

In considering its options, the PCAOB may wish to consider what audit regulators in other countries do. For example, the Canadian Public Accountability Board issues an annual public report with an overview of inspection findings, including common inspection finding themes and questions for audit committees to consider when overseeing external auditors. The PCAOB also may want to consider getting input from stakeholders such as audit committees to evaluate whether PCAOB reports are meeting their information needs.

Meeting the challenge of the evolving technology landscape

We agree that “innovations in data analytics and technology have great potential to improve the efficiency and effectiveness of the financial reporting and audit process.”⁵ This transformative age provides both risks and opportunities for the audit profession, investors, businesses and all other stakeholders. Anticipating, understanding and harnessing technological innovation is more important than ever for all of us.

We therefore support the establishment of the PCAOB's Data and Technology Task Force, organized under the Standing Advisory Group, as an important step in understanding and evaluating the ways in which technology can enhance the effectiveness and efficiency of the audit in order to inform any future PCAOB standard-setting activity. We believe the best public policy outcomes are often achieved when the public and private sector work together, including in forums such as this task force, to benefit from technological advancements.

⁴ 4010 reports are issued under PCAOB Rule 4010, which gives the Board the authority to “at any time, publish such summaries, compilations, or other general reports concerning the procedures, findings, and results of its various inspections as the Board deems appropriate.” Available on the PCAOB website, pcaobus.org/Rules/Pages/Section_4.aspx.

⁵ Ibid., p. 9.

While the creation of the task force is a positive development, we believe the PCAOB will need to consider how it can be even more nimble and agile. To reflect this in the Draft Plan, we suggest that the language of Goal Two be broadened beyond “oversight” activities to reflect a wider range of potential PCAOB actions that can be undertaken in light of emerging risks and opportunities. For example, these should include taking steps to make sure that the Board and staff are abreast of developments that could impact the audit or issuing guidance and re-examining standards based on those developments.

We also support further efforts by the PCAOB, SEC and others to identify the risks and opportunities created by technological developments, particularly those with significant investor impact. A key element of these efforts should focus on providing stakeholders with sufficient understanding of the roles and responsibilities of the parties involved in financial reporting to help manage the expectations gap between investor information needs and what audited financial statements provide. Absent such a step, there is a risk that the expectations gap could expand further. We further encourage the PCAOB to broaden its goals to engage with the SEC and other financial reporting and audit stakeholders to promote an understanding of the scope of the audit as determined by PCAOB standards and explore whether and, if so, how the role of financial reporting, the audit and related standards may need to evolve to address stakeholder needs moving forward.

Stakeholder engagement and communication

We support the goal of building on and enhancing the PCAOB’s proactive stakeholder engagement. Such engagement will improve the PCAOB’s ability to respond to and address new and emerging audit matters. For example, increased interaction with the preparer community and the SEC on standard-setting matters with issuer impact would strengthen standard setting and add to effective implementation.

There are three specific aspects of the proactive stakeholder engagement goal that we suggest the PCAOB consider enhancing.

One stakeholder community that is vital to audit quality moving forward is future auditors who are currently students at universities. The PCAOB can have a positive impact on audit quality now and in the future by promoting the role and relevance of the audit to make sure auditing remains an attractive profession for new entrants. In addition, we encourage the PCAOB to consider how it can actively engage with future auditors. Fast-paced technological developments present opportunities to better explain the importance of high-quality financial reporting and the independent audit to the next generation of auditors. We encourage the PCAOB to publicly discuss how today’s students will help shape the transformation of the audit. The PCAOB could consider steps such as enhancing its visibility and engagement on campuses. We also encourage the PCAOB to work more closely with the academic community and the audit profession to identify the skills that future auditors will need, as well as encourage the development of accounting doctoral faculty.

Engagement and coordination with regulators globally is another area we encourage the PCAOB to emphasize, given its importance to audit quality. As the Draft Plan observes, firms from approximately 90 jurisdictions are registered with the PCAOB. The Draft Plan currently includes an objective “to expand our engagement with other audit regulators around the globe to share perspectives.”⁶ We

⁶ Ibid., p. 10.



support this objective but encourage the PCAOB to take this further to enhance coordination with regulators in other countries on a bilateral and multilateral level. One potential area to consider is whether and how to expand reliance on inspections carried out by non-US audit regulators in appropriate circumstances, which could, over time, enhance the effectiveness and efficiency of the PCAOB's inspection program. The PCAOB's continued active engagement with – and leadership in – the International Forum of Independent Audit Regulators also will support the positive evolution of audit oversight globally, to the benefit of audit quality and investors' interests.

We also believe that the PCAOB should continue to enhance its involvement with audit standard setters around the world, including the International Auditing and Assurance Standards Board. Collaborating with other standard setters will help promote efficiency and consistency with respect to existing standards such as those governing the auditor's report, as well as new projects resulting from business transformation and technological developments. More generally, such collaboration will also help advance audit quality across borders and enhance the value users of financial statements around the world place on the independent audit. Given the pace of change in the audit environment and our interconnected markets, it is more important than ever that we remain committed to exchanging ideas and learning from developments unfolding in the marketplace and in jurisdictions around the world.

Closing

We appreciate the opportunity to share our perspectives, and we would be pleased to discuss our comments with the Board or its staff at your convenience. We look forward to continuing to engage with the Board and its staff in support of a shared commitment to continuously improve audit quality.

Very truly yours,

CC:

PCAOB

William D. Duhnke, III, Chair
J. Robert Brown, Jr., Board Member
Duane M. DesParte, Board Member
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James G. Kaiser, Board Member

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