

Office of Economic and Risk Analysis – An Overview

Michael Gurbutt and Patrick Kastein
Office of Economic and Risk Analysis
PCAOB SEIAG Meeting
November 2, 2022

OVERVIEW

- PCAOB Office of Economic and Risk Analysis (OERA)
 - Formed in May 2017; merged the Center for Economic Analysis (CEA) with the Office of Research and Analysis (ORA)
- Responsible for a diverse portfolio of functions, united around a common goal of enabling high-quality, data-driven analysis:
 - Economic analysis in support of standard-setting and rulemaking
 - Post-implementation review of new or revised standards and rules
 - Risk analysis in support of DRI & DEI
 - Economic modeling
 - Business intelligence
 - Research and relationships with academia

Economic Analysis



ECONOMIC ANALYSIS – OVERVIEW

- Rigorous, evidence-informed analyses of PCAOB proposed and final standards and rules for the benefit of investors
 - Preliminary economic analysis in proposing release
 - Welcome the public's comments, and particularly data
 - Final economic analysis in adopting release
 - Informs the Board but also the SEC's approval process
- To the extent possible, perform quantitative analysis using various data sources:
 - Information from PCAOB inspections and filings
 - SEC filings, other regulatory data
 - Third-party data feeds

ECONOMIC ANALYSIS – STEPS

- Follow our 2014 Staff Guidance on Economic Analysis in PCAOB Standard-Setting
 - Informed by SEC's 2012 Current Guidance on Economic Analysis in SEC Rulemakings
 - Follows executive branch best practices (e.g., OMB Circular A-4)
- Four steps in every economic analysis:
 - Establish the baseline – current state of the world
 - Identify the need for rulemaking (e.g., market failure)
 - Assess the benefits, costs, and other effects of the chosen regulatory approach
 - Evaluate reasonable alternatives

ECONOMIC ANALYSIS – SPECIAL CASES

- Application of a standard to audits of Emerging Growth Companies (EGCs)
 - OERA's analysis supports the Board's decision-making (and in turn the SEC's determination) under the Jumpstart our Business Startups Act
 - OERA Business Intelligence team prepares an annual White Paper regarding EGCs and their auditors to help support this analysis

ECONOMIC ANALYSIS – EXAMPLES

- Recent examples of PCAOB economic analyses include:
 - Estimates & Specialists Standards
 - Leveraged inspections data to inform the analysis
 - Other Auditors Standard
 - Made robust use of inspections as well as Form AP data
 - Holding Foreign Companies Accountable Act Rulemaking
- Current work:
 - Performing research and developing economic analyses to support the standard-setting projects on OCA's standard-setting agenda

ECONOMIC ANALYSIS – STAFFING

- Currently have 8 full-time employees devoted to standard-setting:
 - 6 PhD economists.
 - 2 senior research analysts
- Assisted by OERA staff from other disciplines as needed:
 - Economists on post-implementation review team
 - Audit & accounting specialists
 - Business intelligence analysts
 - Academic fellows
 - Chief Counsel

Post-Implementation Review

A decorative graphic consisting of a grid of blue circles of varying sizes, arranged in a pattern that appears to recede into the distance, set against a dark blue background.

POST-IMPLEMENTATION REVIEW – OBJECTIVES

- OERA conducts post-implementation review (PIR) to evaluate the overall effect of new or revised standards or rules
 - What were the expected benefits and are they being achieved?
 - What were the costs associated with implementation?
 - Did any unintended consequences (foreseen or unforeseen) manifest?
- Post-implementation review can:
 - Identify the need for guidance on the standard/rule
 - Identify a need for future standard-setting (e.g., amendments)
 - Increase awareness of standards
 - Clarify uncertainties that were identified during the rulemaking

PIR – SELECTION

- Any new or revised standard or rule could in theory be the subject of a PIR
- We consider, when choosing a standard or rule for PIR:
 - Whether the Board or the SEC directed us to study it
 - e.g., SEC approval order for Auditor's Reporting Model
 - Expected magnitude and degree of uncertainty around the economic impacts (benefits, costs, unintended consequences)
 - Research design and data availability
 - Potential uses of the analysis

PIR – METHODS

- To evaluate benefits, costs, or unintended consequences, we have several tools in our toolkit:
 - Stakeholder outreach — surveys, targeted interviews, etc.
 - Econometric analysis, if data is available
 - Public request for comment
- We inform the public about the outcome of our analysis through:
 - Preparation of a Board Report with high-level findings or action items
 - Issuance of staff white papers with detailed findings

PIR – INTERIM ANALYSIS

- PIRs generally should take place several years after the rule's effective date.
 - Enables more complete assessment of economic effects, including those that may take some time to manifest
- Recent use of interim analysis to monitor rules as they are implemented
 - Leverages PIR skillset to generate preliminary findings
 - Can provide early warning signal in time to make adjustments

PIR – RECENT WORK

- Completed PIRs: *AS 1220, Engagement Quality Review*
- Work in progress:
 - Critical Audit Matters Interim Analysis:
 - Analysis #1: implementation by Large Accelerated Filers
 - 1 Board Report & 2 staff white papers
 - Available on our website currently
 - Analysis #2: implementation by all issuers subject to the requirements
 - Expected by end of year
 - Estimates & Specialists Interim Analysis
 - Expected by end of year

PIR – STAFFING

- Currently have 6 full-time PhD economists devoted to PIR work
- Assisted by OERA staff from other disciplines as needed:
 - Research Analysts
 - Academic Fellows
 - Chief Counsel

Risk Analysis



RISK ANALYSIS – OBJECTIVES

- Supports DRI's inspection selection process by:
 - Analyzing economic trends and corporate transactions, along with industry, accounting, and issuer audit-level risks
 - Identifying higher-risk issuer audits, and suggested focus areas within those audits, for DRI's consideration
 - Highlighting areas of emerging risk (e.g., SPACs)
- Supports DEI's case selection process by providing analyses that assist with the identification of issues for further investigation

RISK ANALYSIS – STAFFING

- Currently have 9 full-time employees devoted to Risk Analysis, including:
 - CPAs
 - Data analyst
- Supported by other areas within OERA, as needed

Economic Modeling



ECONOMIC MODELING – OVERVIEW

- Develop econometric models that can improve the PCAOB's ability to identify systematically issuer financial statements with higher risk of restatement, with the goal of informing DRI's inspection selection process

ECONOMIC MODELING – STAFFING

- Currently have 4 full-time employees devoted to the modeling work:
 - 3 PhD economists
 - 1 data/modeling manager
- Assisted by OERA staff from other disciplines as needed:
 - CPAs
 - Academic fellows
 - Research and data analysts

Business Intelligence



BUSINESS INTELLIGENCE – OBJECTIVES

- BI team is composed of highly experienced analysts skilled at transforming data captured from multiple sources (e.g., firms, third-party data vendors, and PCAOB programs) into datasets, insights, and analysis
 - In 2021, ERA's BI group issued almost 600 reports and analyses in support of PCAOB oversight activities
 - BI provides reports to every division at the PCAOB
- Some reports are periodic/recurring, others are ad hoc:
 - Our complex datasets collect and analyze information for use by DRI staff in the inspection selection process
 - We release an annual EGC white paper to inform standard-setting

BUSINESS INTELLIGENCE – STAFFING

- Currently have 8 full-time employees
 - Subject matter experts on information reported by firms and information reported in SEC filings, with technical skills to aggregate and analyze that information
 - Includes CPAs, data analysts, and financial statement analysts

Research and Academia



ACADEMIC FELLOWS

- Academic Fellowship program
 - Limited number of full-time or part-time, one-year fellowships
 - Objective is to help promote the production of high-quality research into auditing issues and to obtain outside academic perspectives, including by:
 - Producing original academic research papers
 - Assisting permanent staff on priority projects
- Scholars frequently go on to publish papers in top-tier journals
 - 8 published papers and 15 working papers, plus several works in progress

CONFERENCE ON AUDITING AND CAPITAL MARKETS

- Annual academic conference produced by OERA
- The 2022 conference took place on October 20-21, and included panels on:
 - The Auditor's Going Concern Evaluation: Auditor Responsibilities and Market Impacts
 - Developments in the Use of Technology-Based Tools on Audits
 - The IT Environment of Public Companies and Implications for the Audit
 - The Organization of the Audit Market and Implications for Audit Quality
 - Auditor Independence: The Impact of Non-Audit Services on Audit Outcomes
- 454 registered attendees

QUESTIONS

