May 11, 2020

Members of the Public Company Accounting Oversight Board
comments@pcaobus.org

RE: Interim Analysis No. 2020-01, Critical Audit Matter Requirements

Dear Board Members:

We are pleased to respond to the Board's *Request for Comment on Interim Analysis No. 2020-01, Critical Audit Matter Requirements*, dated April 17, 2020.

Overall Commentary:

We commend the Board on actions taken to make the auditor's report more relevant to investors and other financial statement users by requiring more information about the auditor and the audit including reporting, "any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved especially challenging, subjective, or complex auditor judgment" (CAMs – AS 3101, ¶ 11).

As part of our recently concluded research study, "Critical Audit Matters – Early Perceptions," we sent surveys to the chief financial officers, audit engagement partners, and audit committee chairs of U.S. large accelerated issuers with fiscal years ending between June 30, 2019 and July 31, 2019 (n = 62 issuers). The purpose of the survey was to gain insight into the CAM identification and reporting process. We also inquired about the impact of CAM disclosures on audit effectiveness, efficiency, quality, and fees.

Three major conclusions were drawn from the survey results. First, the CAM identification and reporting process results in higher audit fees. Second, concerns expressed by commenters on the proposed new auditor's report about attention being diverted from the audit and possible negative impacts on audit quality appear to be unfounded. Third, chief financial officers, audit engagement partners, and audit committee members participating in the process see little, if any, value added by reporting CAMs.

Although the number of survey respondents is small (n = 20, 18 unique issuers), triangulation of the survey's findings with related archival data suggests reliability of our findings among these stakeholders of the largest issuers.

The question-specific commentary provided below draws from data collected from the study's survey respondents (chief financial officers - CFOs, audit engagement partners - AEPs, and audit committee chairs - ACCs).

Question-specific Commentary (question numbers are as reported in the *Request for Comment*)**:**

4. Have preparers and audit committees experienced any changes in the financial reporting process as a consequence of CAM communications in the auditor's report? For example, has the communication of CAMs led to changes in controls or practices around financial reporting and disclosure? Did CAM communications result in any reconsideration of, or changes to, disclosures management made in company filings (e.g., notes to the financial statements, critical accounting estimates, MD&A, or risk factors)?

Related to this question, our survey asked, "To what extent do CAMs divert resources of your organization from other accounting and/or auditing matters?" The mean response to this question was 4.0 for AEPs, 2.1 for CFOs, and 3.2 for ACCs (scale of: 1 = none, 4 = moderate, 7 = substantial). Reports by AEPs are statistically higher than those of CFOs. We interpret these data as the CAM identification and reporting process being conducted largely between AEPs and ACCs.

7. Did CAM requirements lead to changes in communications between auditors, audit committees, or preparers? For instance, were there changes in the nature or frequency of communications during the audit process? Did audit committee members ask more or different types of questions? Was there more focus on matters that were identified as CAMs?

Related to this question, our survey asked, "To what degree have you had input on the language of CAMs?" The mean response to this question was 6.3 for AEPs, 2.4 for CFOs, and 3.6 for ACCs (scale of: 1 = none, 4 = moderate, 7 = substantial). Statistically higher responses by AEPs compared to both CFOs and ACCs, confirm there was relatively little input of the descriptions used by auditors in the identification and resolution of CAMs.

8. Based on your experience as a preparer or auditor, what were the most significant activities that led to CAM-related costs? First, please describe each activity, including any preparatory activities (e.g., pilots or dry-runs). Next, please estimate the total costs related to CAM requirements in hours (and external spend, if applicable) for each of those activities for each calendar year from 2017-2019 and the period January-April 2020, distinguishing, to the extent possible, between costs related to preparatory activities and costs related to recurring activities. Finally, for any activities that will be recurring, state whether you believe the costs will increase, decrease, or not change for each activity in future years.

Related to this question, our survey asked, "To what extent do you believe CAMs influence audit fees? The mean response to this question was 5.0 for AEPs, 4.9 for CFOs, and 5.2 for ACCs (scale of: 1 = substantially reduces, 4 = no impact, 7 = substantially increases). These scores, which are statistically higher than "no impact," suggest audit fees have likely increased because of CAM reporting. It is unclear whether this increase is related solely to the initiation of CAM reporting or will be continuing.

9. From your perspective as an auditor or preparer, at which stages of the audit process did most of your activities related to CAMs occur? Did the majority of your effort occur before or

after the company's fiscal year end? What factors contributed to the timing of your efforts related to CAMs?

Related to this question, our survey asked, "Approximately how long ago were CAMs first discussed between the CFO, audit engagement partner, and audit committee chair?" The mean response to this question was 4.8 for AEPs, 3.0 for CFOs, and 5.0 for ACCs (scale of: 1 = < 6 months, 4 = one year, 7 = > 2 years). These data add confirmatory evidence that the CAM identification and reporting process is largely an effort of AEPs and ACCs. Both AEPs and ACCs began their consideration of CAMs more than one year before they were required to be reported.

We hope our comments add insight to the Board's Interim Analysis of CAMs.

Respectfully submitted,

Brian Daugherty, Ph.D., CPA, Associate Professor
University of Wisconsin – Milwaukee
daughert@uwm.edu

Denise Dickins, Ph.D., CPA, CIA, Professor
East Carolina University
dickinsd@ecu.edu

Marshall K. Pittman, Ph.D., CPA, CMA, Professor
University of Texas at San Antonio
marshall.pitman@utsa.edu

Wayne A. Tervo, Ph.D., CPA, Associate Professor
Murray State University
wtervo@murraystate.edu