

# Exhibit 1

## **1 American Accounting Association**

September 16, 2016 Letter from American Accounting Association

June 27, 2016 Letter to American Accounting Association

## **2 American Institute of Certified Public Accountants**

September 27, 2016 Letter from American Institute of Certified Public Accountants

June 27, 2016 Letter to American Institute of Certified Public Accountants

## **3 National Association of State Boards of Accountancy**

September 12, 2016 Letter from National Association of State Boards of Accountancy

June 27, 2016 Letter to National Association of State Boards of Accountancy

## **4 Public Company Accounting Oversight Board**

September 16, 2016 Letter from Public Company Accounting Oversight Board

Attached Summary Chart (noted in Letter as "Tab 1")

Attached Board Member Franzel's April 2016 Article (noted in Letter as "Tab 2")

PCAOB Standing Advisory Group Meeting, October 13-14, 2010

June 27, 2016 Letter to Public Company Accounting Oversight Board

## **5 United States Securities and Exchange Commission**

October 13, 2016 Letter from United States Securities and Exchange Commission

June 27, 2016 Letter to United States Securities and Exchange Commission

## **6 Department of the Treasury**

August 15, 2016 Letter to Department of the Treasury

**1**

**American Accounting  
Association**



September 16, 2016

Parveen Gupta  
Lynn Turner  
Committee Co-Chairs  
Investor Advisory Group  
Public Company Oversight Board  
Working Group on the U.S. Treasury Advisory  
Committee on the Auditing Profession

Dear Parveen and Lynn,

In reference to your request for a response for the Investor Advisory Group of the PCAOB, with respect to the Advisory Committee on the Auditing Profession (ACAP) recommendations, you will find below and attached potentially useful resources created by the Pathways Commission on Accounting Higher Education, the American Accounting Association, and several other organizations.

Recommendation 5 of the "Final Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury" (2008) encouraged: "...the AICPA and the AAA jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession". (p. VI:25)

The AICPA and AAA jointly formed The Pathways Commission on Accounting Higher Education: Charting a National Strategy for the Next Generation of Accountants – now commonly referred to as "The Pathways Commission", "to study the future structure of higher education for the accounting profession and develop recommendations for educational pathways to engage and retain the strongest possible community of students, academics, practitioners, and other knowledgeable leaders in the practice and study of accounting." (The Pathways Commission, 2012, p. 9).

A wide range of individuals and organizations participated in the work of the Pathways Commission, many of them working in parallel in other organizations and institutions on projects aligned with the ideas being explored by the Commission. Included here (attached and with links provided) are the full set of reports published by the Pathways Commission. As well, the summary below provides links to these reports posted online as part of the extensive collection of resources created by, and shared widely throughout, the project at [pathwayscommission.org](http://pathwayscommission.org) and [pathwaysinspired.org](http://pathwaysinspired.org). The Commission's substantive body of work - designed and created by academics and practitioners from a wide range of institutions, companies, and firms - from across the learned profession of accounting broadly defined – resulted from conversations and plans sparked by the ACAP report.

In parallel, and building on synergies with the ongoing work of the Pathways Commission, the Board of Directors and Council of the American Accounting Association (AAA), began a new phase of strategic planning titled "Sharpening our Vision" (see attached, "The AAA Centers for Advancing Accounting"), resulting in plans to create Centers for Advancing Accounting

focusing in four areas: education, research, practice, and the public interest. With research and recommendations from its member leadership, and building on insights gained through co-sponsoring the Pathways Commission, the AAA Board approved plans to launch the new strategy with the Center for Advancing Accounting Education.

The three attached appendices include reports and online resources providing an overview of the work of the Pathways Commission, potentially useful online resources, and resources organized by ACAP recommendation. An electronic version with the working links will follow, to allow ease of use of the reference links.

All the best,

A handwritten signature in cursive script, appearing to read "Tracey E. Sutherland".

Tracey E. Sutherland, PhD  
Executive Director

## Appendix A: The Pathways Commission

### **Pathways Commission reports included (and their online links)**

The Pathways Commission. (2015). *Implementing the Recommendations of The Pathways Commission*. August, 2015.

<http://commons.aaahq.org/posts/b81024f4c3>

- Appendix (Excel file attached)  
An inventory of Resources by the Large Firms – for faculty engagement with practice

The Pathways Commission. (2015). *In Pursuit of Accounting's Curricula of the Future*. November, 2015.

<http://commons.aaahq.org/posts/d4ca98263a>

The Pathways Commission. (2015). *A Survey of Support for Teaching, Recognition of High Quality Teaching, and Use of Teaching Portfolios in Accounting Programs*. November, 2015.

<http://commons.aaahq.org/posts/24b8aa3bc1>

The Pathways Commission. (2014). *Proposal for a National Center for Accounting Education Excellence*. June, 2014.

<http://www2.aaahq.org/images/PathwaysReport3.pdf>

The Pathways Commission. (2014). *How Integrating Professionally Oriented Faculty Enhances an Institution's Mission*. June, 2014.

<http://www2.aaahq.org/images/PathwaysReport1.pdf>

- The Pathways Commission asked departments/institutions to adopt the leading practice principles for integrating POF, and openly acknowledge their support in the journey to build a learned profession -  
<http://commons.aaahq.org/posts/3e84f870d7>

The Pathways Commission. (2014). *An Examination of Non-Traditional Doctoral Education*. June, 2014.

<http://www2.aaahq.org/images/PathwaysReport2.pdf>

The Pathways Commission. (2014). *Implementing the Recommendations of the Pathways Commission: Year Two*. August, 2014.

<http://commons.aaahq.org/posts/d4a609b8e4>

The Pathways Commission. (2013). *Implementing Recommendations for the Future of Accounting Education: The First Year Update*. August, 2013.

<http://commons.aaahq.org/posts/6153324d1b>

The Pathways Commission. (2012). *The Pathways Commission: Charting a National Strategy for the Next Generation of Accountants*. July, 2012.

<http://commons.aaahq.org/groups/2d690969a3/summary>



## Appendix B: Resources available online

Pathways Commission Homepage

<http://commons.aaahq.org/groups/2d690969a3/summary>

Pathways Commission supplemental information

Pathways Vision Model: THIS is Accounting

<http://commons.aaahq.org/hives/a943df3efc/summary>

- See also video description of the Vision Model and its background by key leaders of the development team, G. Peter Wilson and Carolyn Wilson (Boston College) on the Pathways Commission homepage - <http://commons.aaahq.org/groups/2d690969a3/summary>
- Pete and Carolyn led a team of speakers highlighting the Vision Model for AAA meetings – serving as the national speakers for the AAA Conference on Teaching and Learning (CTLA) traveling team for AAA Regions. The Vision Model has been a key element of their online tools:
  - Related resource – the Wilson’s online resources at *Navigating Accounting* - <http://www.navigatingaccounting.com>
- The Pathways Vision Model is now being adopted in accounting textbooks by at least two publishers (Pearson and McGraw Hill).
- PowerPoint deck designed to help those who want to understand the concepts behind the Pathways Vision Model. Based on a presentation made at the American Accounting Association’s annual meeting - <http://commons.aaahq.org/posts/e9e699b00f>

Pathway to Academic for Accounting Professionals Webcast (10/2015)

<http://commons.aaahq.org/posts/2c8f27a1df>

Pathways Inspired Homepage

<http://commons.aaahq.org/groups/0fa82ab56d/summary>

Pathways Data Collection - <http://commons.aaahq.org/groups/2d690969a3/summary>

Recommendation 1

- Professional-oriented faculty
- Professionally-oriented faculty – Department Chairs

Recommendation 2

- Nontraditional programs – Directors
- Nontraditional programs – Faculty
- Nontraditional programs – Students

Recommendation 3

- Teaching Quality Survey

Recommendation 4

- Technology Survey

Recommendation 5

- AP Accounting – Survey of Academic Leaders - <http://commons.aaahq.org/posts/8ca8859e31>
- Accounting Pilot & Bridge Project - <http://commons.aaahq.org/posts/87ccab3215>

Recommendation 6

- Accounting Programs Survey

### American Accounting Association

The AAA Centers for Advancing Accounting - overview document attached.

<http://aaahq.org/Portals/0/documents/centers/The%20Centers%20for%20Advancing%20Accounting%202012%202014%2014.pdf>

#### Potential resources

The AAA holds more than 25 meetings annually, and publishes 16 journals. These resources created by members and the larger accounting community are key sources of sharing new knowledge and insights related to teaching, research and practice within the learned profession of accounting. A few examples of work in these areas that parallel ACAP recommendations are included below.

#### AAA Sharpening our Vision (SOV)

<http://aaahq.org/About/Sharpening-Our-Vision>

#### AAA Meetings Archive

<http://aaahq.org/Meetings/2016/Archive>

- Beginning in 2012, SOV strategic discussions began influencing AAA Annual Meeting programs (see attached example list of Pathways Commission panels, 2012).
- In accordance with its role as co-sponsor of the Pathways Commission, the AAA has incorporated related topics and activities into its meetings, which became an important point of informing and engaging the community about Commission projects. AAA meeting archives highlight the inclusion of the work of the Commission during panels at Annual Meetings, Region Meetings, the Conference on Teaching and Learning in Accounting (CTLA), and Section meetings. The Accounting Program Leaders Group (APLG) was a key point of engaging and seeking input for the Commission from program leaders, department chairs, and deans. Members involved in the work of the Commission were regularly asked to speak at related events including those of NASBA, AACSB, state societies, and TACTYC (Teachers of Accounting at Two-Year Colleges), etc.

#### The AAA/J. Michael and Mary Anne Cook/Deloitte Foundation Prize

<http://aaahq.org/Education/Awards/The-J-Michael-and-Mary-Anne-Cook-Prize>

- As part of the AAA Center for Advancing Accounting Education, aligning with Pathways Recommendation 3, and with the support of Michael and Mary Anne Cook, the “Cook Prize” was launched in 2015 as the foremost recognition of faculty who consistently demonstrate the attributes of a superior teacher in the discipline of accounting. The Prize is intended to recognize, inspire and motivate achieving the status of a superior teacher. Each year up to three awards of \$25,000 each can be made in the categories of graduate, undergraduate, and two-year accounting degree programs.



## Appendix C: Resources aligned with ACAP Recommendations

Below are information and resources about example projects of the Pathways Commission (co-sponsored by the AICPA and AAA), and American Accounting Association (with goals parallel to those of ACAP Human Capital recommendations).

### Human Capital Recommendations

**Recommendation 1. Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high quality audits.**

- a) Regularly update the accounting certification examinations to reflect changes in the accounting profession, its relevant professional and ethical standards, and the skills and knowledge required to serve increasingly global capital markets.
- b) Reflect real world changes in the business environment more rapidly in teaching materials.
- c) Require that schools build into accounting curricula current market developments.

### **Potential resources**

#### Pathways Commission

- The Pathways Commission. (2015). *In Pursuit of Accounting's Curricula of the Future*. November, 2015 - <http://commons.aaahq.org/posts/d4ca98263a>
- Pathways Vision Model: THIS is Accounting - <http://commons.aaahq.org/hives/a943df3efc/summary>
- Addressing Pathways Commission Recommendation 1, encouraging practice/educator interactions, the largest five public accounting firms have partnered with AAA Sections to expand the highly successful audit educator "bootcamp" model created by the Auditing Section of the AAA. In 2015 the Auditing, Information Systems, and Tax Sections held these practice update bootcamps, providing faculty development opportunities and teaching materials. The program will continue into 2016-17.
  - Audit Educator's Bootcamp - <http://aaahq.org/Meetings/2015/Audit-Educators-Bootcamp>
- The Pathways Commission collated core competency frameworks across accounting organizations - <http://commons.aaahq.org/posts/a3470e7ffa>

#### American Accounting Association

- AAA Big Thinker Conferences - launched as part of the Centers for Advancing Accounting, an implementation of the Sharpening our Vision strategy, and beginning with the topic of big data and analytics. With the goal of identifying key issues engaging the broad learned profession of accounting practice, education, and research - a long-term goal is conferences attracting 50/50 academics and practitioners. Year 1 was a good start with 30% practice and 70% academic participants - Year 2 has increased to 40% practice participants. The interactive



program includes case analysis and teaching and research resources on site – and builds resources and webinars through the year.

- Accounting IS Big Data, San Francisco, September, 2016 - <http://aaahq.org/Meetings/2016/Accounting-Is-Big-Data-Conference>
- Accounting IS Big Data, New York City, September, 2015 - <http://commons.aaahq.org/groups/cea5c9d7d1/summary>
- Conference on Teaching and Learning (and traveling CTLA team for AAA Region Meetings) - <http://aaahq.org/Meetings/2016/Annual-Meeting/Program/CTLA-Program>
- Publications – AAA journals are a key point for sharing insights and findings related to research, teaching and practice issues. As an example, focusing on the impact of big data on the accounting profession, special issues/forums are being published across the AAA collection. A few examples
  - *Accounting Horizons* – Forum: Big Data, June 2015, Vol. 29, No. 2. Edited by Paul Griffin and Arnie Wright.
  - Helen Brown-Liburd and Miklos A. Vasarhelyi (2015) Big Data and Audit Evidence. *Journal of Emerging Technologies in Accounting*: December 2015, Vol. 12, No. 1.
  - *Journal of Information Systems*: Fall 2013, Vol. 27, No. 2.
  - *Journal of Emerging Technologies in Accounting*: December 2016, Vol. 13.
- *Issues in Accounting Education* provides members with instructional resources and cases reflecting real-world environments – an example - <http://aaajournals.org/toc/iace/30/4>
- Partnering with the Financial Accounting Foundation and COSO, “Academic Access” to professional-level tools of the FASB Standards Codification and GARS System, and COSO ERM Framework are available to faculty and students through the AAA, and the Center for Advancing Accounting Education is gathering and making available related teaching resources - <http://aaahq.org/Research/FASB-GARS> and <http://aaahq.org/COSO>

### **Other organizations**

#### AACSB

- Business and Accounting Accreditation Standards – supporting concepts developed during the work of the Pathways Commission <http://www.aacsb.edu/~media/AACSB/Docs/Accreditation/Standards/2013-bus-standards-update.ashx>
- AACSB Collective Vision for Business Education - 2016 <http://www.aacsb.edu/~media/ManagementEducation/docs/collective-vision-for-business-education.ashx>

#### Accreditation Council for Business Schools and Programs (ACBSP)

<http://www.acbsp.org>

Accounting Doctoral Scholars Program (ADS) - <http://www.adsphd.org> - AICPA, and largest accounting firms committed more than \$17 million to recruiting PhD students with public accounting experience. New follow-up launching Fall 2016.

#### Institute of Management Accountants (IMA) Competency Framework

<http://www.imanet.org/tools-and-resources/competency-framework>

Building on the work of a joint task force of the Management Accounting Section of the AAA and IMA, the competency framework has been discussed and published twice in *Issues in Accounting Education*. See articles referenced below.

### **Related articles**

The AAA Management Accounting Section and Institute of Management Accountants (IMA) Raef A. Lawson, Edward J. Blocher, Peter C. Brewer, Gary Cokins, James E. Sorensen, David E. Stout, Gary L. Sundem, Susan K. Wolcott, and Marc J. F. Wouters (2014) Focusing Accounting Curricula on Students' Long-Run Careers: Recommendations for an Integrated Competency-Based Framework for Accounting Education. *Issues in Accounting Education*. May 2014, Vol. 29, No. 2, pp. 295-317.

Raef A. Lawson, Edward J. Blocher, Peter C. Brewer, Jan Taylor Morris, Kevin D. Stocks, James E. Sorensen, David E. Stout, and Marc J. F. Wouters (2015) Thoughts on Competency Integration in Accounting Education. *Issues in Accounting Education*. August 2015, Vol. 30, No. 3, pp. 149-171.

### **Recommendation 2. Improve the representation and retention of minorities in the audit profession so as to enrich the pool of human capital in the profession.**

- a) **Recruit minorities into the auditing profession from other disciplines and careers.**
- b) **Institute initiatives to increase the retention of minorities in the profession.**
- c) **Emphasize the role of community colleges in the recruitment of minorities into the auditing profession.**
- d) **Emphasize the utility and effectiveness of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.**
- e) **Increase the numbers of minority accounting doctorates through focused efforts.**

### **Potential resources**

#### Pathways Commission

The Pathways Commission. (2012). *The Pathways Commission: Charting a National Strategy for the Next Generation of Accountants*. July, 2012. p 18-19.

<http://commons.aaahq.org/groups/2d690969a3/summary>

“There are three issues not specifically addressed in this report that the Commission felt compelled to identify: the ACAP recommendation to consider a postgraduate professional school of accounting, detailed recommendations on enhancing diversity in the accounting profession, and the 150-hour educational requirement for accountants.” (18-19)

#### American Accounting Association

- Articles related to the experience of minority students and faculty can be found in *Issues in Accounting Education* and *Accounting Horizons*.
- The Diversity Section of the AAA holds a fall seminar, and contributes sessions to the Annual Meeting program. <http://aaahq.org/Meetings/2015/Diversity-Section/Program>
- AAA participates as a sponsor of the PhD Project, coordinating the Project's meeting of accounting doctoral students in the pre-meeting activities of the Annual Meeting.



## Other resources

AICPA National Commission on Diversity, chaired by Ken Bouyer, EY

- Diversity and Inclusion Webcast Series - <http://www.aicpa.org/CAREER/DIVERSITYINITIATIVES/Pages/DiversityInitiative.s.aspx>
- Accounting Inclusion Maturity Model - <http://www.aicpa.org/CAREER/DIVERSITYINITIATIVES/Pages/DiversityInitiative.s.aspx>

The PhD Project

<http://www.phdproject.org>

**Recommendation 3. Ensure a sufficient robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high quality audits.**

- Increase the supply of accounting faculty through public and private funding and raise the number of professionally qualified faculty that teach on campuses.**
- Emphasize the utility and effectiveness of cross-sabbaticals.**
- Create a variety of tangible and sufficiently attractive incentives that will motivate private section institutions to fund both accounting faculty and faculty research, to provide practice materials for academic research and for participation of professionals in behavioral and field study projects, and to encourage practicing accountants to pursue careers as academically and professionally qualified faculty.**

## **Potential resources**

### Pathways Commission

The Pathways Commission. (2014). *How Integrating Professionally Oriented Faculty Enhances an Institution's Mission*. June, 2014.

<http://www2.aaahq.org/images/PathwaysReport1.pdf>

- The Pathways Commission asked departments/institutions to adopt the leading practice principles for integrating POF, and openly acknowledge their support in the journey to build a learned profession - <http://commons.aaahq.org/posts/3e84f870d7>

The Pathways Commission. (2014). *An Examination of Non-Traditional Doctoral Education*. June, 2014.

<http://www2.aaahq.org/images/PathwaysReport2.pdf>

### American Accounting Association

Coordination with funders of accounting research: AICPA/CIMA, IMA, PCAOB, CAQ and others to share information about opportunities for research funding and data access.

Doctoral consortia are held by most AAA Sections and at the AAA national level.

Articles are regularly published on the topic of faculty work - for example:



Douglas M. Boyle, Brian W. Carpenter, and Dana R. Hermanson (2015) The Accounting Faculty Shortage: Causes and Contemporary Solutions. *Accounting Horizons*: June 2015, Vol. 29, No. 2, pp. 245-264.

Douglas M. Boyle, Dana R. Hermanson, and Michael O. Mensah (2011) Addressing the Accounting and Auditing Faculty Shortage: Practitioners' Perceptions of Academia. *Current Issues in Auditing*: June 2011, Vol. 5, No. 1, pp. A70-A85.

Trapnell, J. E., N. Mero, J. R. Williams, and G. W. Krull, Jr. (2009) The accounting doctoral shortage: Time for a new model. *Issues in Accounting Education*. 24 (4): 427–432.

Carcello, J. V. (2008) Human capital challenges facing the public company auditing profession. *Current Issues in Auditing*. 2 (1): C1–C12.

R. David Plumlee (Chairman), Steven J. Kachelmeier, Silvia A. Madeo, Jamie H. Pratt, and George Krull (2006) Assessing the Shortage of Accounting Faculty. *Issues in Accounting Education*: May 2006, Vol. 21, No. 2, pp. 113-125.

#### Other resources

Accounting Doctoral Scholars Program (ADS) - <http://www.adsphd.org> - AICPA and largest accounting firms committed more than \$17 million to recruiting PhD students with public accounting experience. New follow-up launching Fall 2016.

Annual CAQ Symposium – designed to bring together practice leaders and audit research scholars for discussion of important issues and exploration of how research can inform those issues <http://www.thecaq.org/research/caq-annual-symposium>

#### **Recommendation 4. Develop and maintain consistent demographic and higher education program profile data.**

#### **Potential resources**

##### Pathways Commission

Pathways data collection - <http://commons.aaahq.org/groups/2d690969a3/summary>

##### American Accounting Association

AAA maintains the online Hasselback Database of accounting faculty  
<http://www.hasselback.org>

Leslie, D. W. 2010. Accounting in Community Colleges: Who Teaches, Who Studies? A report of the American Accounting Association, Sarasota, FL.  
[http://aaahq.org/Portals/0/documents/resources/FacultyTrends\\_2Year.pdf](http://aaahq.org/Portals/0/documents/resources/FacultyTrends_2Year.pdf)

Leslie, D. W. 2009. Trends in Non-Tenure Eligible Accounting Faculty, 1993–2004. A report of the American Accounting Association, Sarasota, FL.  
<http://aaahq.org/Portals/0/documents/resources/LeslieReport2.pdf>

Leslie, D. W. 2008. Accounting Faculty in U.S. Colleges and Universities: Status and Trends, 1993–2004. A report of the American Accounting Association, Sarasota, FL.  
<http://aaahq.org/Portals/0/documents/resources/AccountingFacultyUSCollegesUniv.pdf>

**Recommendation 5. Encourage the AICPA and the AAA jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession.**

The AICPA and AAA jointly formed The Pathways Commission on Accounting Higher Education: Charting a National Strategy for the Next Generation of Accountants – now commonly referred to as “The Pathways Commission”, “to study the future structure of higher education for the accounting profession and develop recommendations for educational pathways to engage and retain the strongest possible community of students, academics, practitioners, and other knowledgeable leaders in the practice and study of accounting.” (The Pathways Commission, p. 9)

Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession

June 27, 2016

Tracey Sutherland  
Executive Director  
American Accounting Association  
5717 Bessie Drive  
Sarasota, FL 34233-2399

Dear Executive Director Sutherland:

In 2007 the U.S. Secretary of the Treasury, the Honorable Henry M. Paulson, Jr., announced and appointed an Advisory Committee on the Auditing Profession (ACAP) "...to consider and develop recommendations relating to the sustainability of the auditing profession." Secretary Paulson appointed twenty one members to the Committee, with a variety of backgrounds including business executives and corporate board members, an accounting academic, former Securities and Exchange Commission (SEC) and Federal Reserve Chairmen, former SEC chief accountants, auditors, investors and attorneys. The Public Company Accounting Oversight Board (PCAOB) Chairman served as an observer to the Committee. A year later in October 2008, the ACAP issued its recommendations.

The PCAOB Investor Advisory Group (IAG) has benefited, as we hope the PCAOB board members and staff have, from the discussions at the IAG meetings in past years. We again look forward to our next meeting on October 27, 2016. At that meeting, a working group of the IAG will be making a presentation to the members of the PCAOB with respect to the progress that has been made in the intervening eight years, on the recommendations of the ACAP. Accordingly, the working group is diligently undertaking to identify the actions taken to date by each entity to which the recommendations were addressed, as well as what obstacles, if any, they have faced in addressing the ACAP recommendations.

To that end, the working group would appreciate it if the American Accounting Association or its staff, could provide a response to the working group, with respect to the ACAP recommendations to the PCAOB in the attached Appendix A, which have been highlighted. (A similar request is being sent to each entity that the ACAP directed its recommendations to.) In particular, if the response could set forth the steps or actions taken to address and implement the recommendations, and when they were taken, would be most useful. This would include either interim or final actions. Such a response would be helpful in ensuring our report to the PCAOB is as comprehensive as possible. In order to adequately consider the response, it would be appreciated if it could be received by no later than September 15, 2016. You can address it to the working group co-chair, Parveen Gupta, Lehigh University, 621 Taylor Street, College of

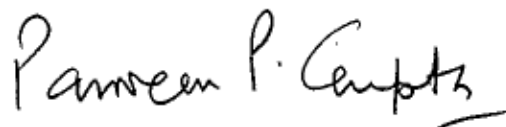


Business and Economics, Lehigh University, Bethlehem PA, 18015. Please do not hesitate to Call Mr. Gupta (610-758-3443) or Mr. Turner (303-956-4895) if you have any questions.

This project is being undertaken by the IAG working group and its members. As such, it is not a project being undertaken by the PCAOB or its staff. However, we hope it will result in a report that is informative and helpful to the PCAOB in its endeavors.


Again, we greatly appreciate your support.

Sincerely,



Parveen Gupta

Investor Advisory Group  
Working Committee Co-Chair



Lynn E. Turner

Investor Advisory Group  
Working Committee Co-Chair

## APPENDIX A

### U.S. Treasury Advisory Committee on the Auditing Profession

October, 2008 Report

Recommendations made to the Securities and Exchange Commission and Others

### Advisory Committee on the Auditing Profession Final Report

#### Human Capital Recommendations

- ✓ **Recommendation 1.** Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high quality audits.
  - ✓ (a) Regularly update the accounting certification examinations to reflect changes in the accounting profession, its relevant professional and ethical standards, and the skills and knowledge required to serve increasingly global capital markets.
  - ✓ (b) Reflect real world changes in the business environment more rapidly in teaching materials.
  - ✓ (c) Require that schools build into accounting curricula current market developments.
- ✓ **Recommendation 2.** Improve the representation and retention of minorities in the auditing profession so as to enrich the pool of human capital in the profession.
  - ✓ (a) Recruit minorities into the auditing profession from other disciplines and careers.
  - ✓ (b) Institute initiatives to increase the retention of minorities in the profession.
  - ✓ (c) Emphasize the role of community colleges in the recruitment of minorities into the auditing profession.
  - ✓ (d) Emphasize the utility and effectiveness of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.
  - ✓ (e) Increase the numbers of minority accounting doctorates through focused efforts.

✓ **Recommendation 3.** Ensure a sufficiently robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high quality audits.

✓ (a) Increase the supply of accounting faculty through public and private funding and raise the number of professionally qualified faculty that teach on campuses.

✓ (b) Emphasize the utility and effectiveness of cross-sabbaticals.

✓ (c) Create a variety of tangible and sufficiently attractive incentives that will motivate private sector institutions to fund both accounting faculty and faculty research, to provide practice materials for academic research and for participation of professionals in behavioral and field study projects, and to encourage practicing accountants to pursue careers as academically and professionally qualified faculty.

✓ **Recommendation 4.** Develop and maintain consistent demographic and higher education program profile data.

✓ **Recommendation 5.** Encourage the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession.

### **Firm Structure and Finances Recommendations**

**Recommendation 1.** Urge the Securities and Exchange Commission (SEC), and Congress as appropriate, to provide for the creation by the Public Company Accounting Oversight Board (PCAOB) of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.

**Recommendation 2.** Encourage greater regulatory cooperation and oversight of the public company auditing profession to improve the quality of the audit process and enhance confidence in the auditing profession and financial reporting.



(a) Institute the following mechanism to encourage the states to substantially adopt the mobility provisions of the Uniform Accountancy Act, Fifth Edition (UAA): If states have failed to adopt the mobility provisions of the UAA by December 31, 2010, Congress should pass a federal provision requiring those states to adopt these provisions.

(b) Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.

(c) Urge the states to create greater financial and operational independence of their state boards of accountancy.

**Recommendation 3.** Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze, explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.

**Recommendation 4.** Urge the SEC to amend Form 8-K disclosure requirements to characterize appropriately and report every public company auditor change and to require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audit clients.

**Recommendation 5.** Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor's standard reporting model. Further, urge that the PCAOB and the SEC clarify in the auditor's report the auditor's role in detecting fraud under current auditing standards and further that the PCAOB periodically review and update these standards.

**Recommendation 6.** Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report.

**Recommendation 7.** Urge the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating (a) information required by the EU's Eighth Directive, Article 40 Transparency Report deemed appropriate by the PCAOB, and (b) such key indicators of audit quality and effectiveness as determined by the PCAOB in accordance with Recommendation 3 in Chapter VIII [Concentration and Competition] of this Report. Further, urge the PCAOB to require that, beginning in 2011, the larger auditing firms file with the PCAOB on a confidential basis audited financial statements.

## **Concentration and Competition Recommendations**

**Recommendation 1.** Reduce barriers to the growth of smaller auditing firms consistent with an overall policy goal of promoting audit quality. Because smaller auditing firms are likely to become significant competitors in the market for larger company audits only in the long term, the Committee recognizes that Recommendation 2 will be a higher priority in the near term.

(a) Require disclosure by public companies in their registration statements, annual reports, and proxy statements of any provisions in agreements with third parties that limit auditor choice.

(b) Include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements.

**Recommendation 2.** Monitor potential sources of catastrophic risk faced by public company auditing firms and create a mechanism for the preservation and rehabilitation of troubled larger public company auditing firms.

(a) As part of its current oversight over registered auditing firms, the PCAOB should monitor potential sources of catastrophic risk which would threaten audit quality.

(b) Establish a mechanism to assist in the preservation and rehabilitation of a troubled larger auditing firm. A first step would encourage larger auditing firms to adopt voluntarily a contingent streamlined internal governance mechanism that could be triggered in the event of threatening circumstances. If the governance mechanism failed to stabilize the firm, a second step would permit the SEC to appoint a court-approved trustee to seek to preserve and rehabilitate the firm by addressing the threatening situation, including through a reorganization, or if such a step were unsuccessful, to pursue an orderly transition.

✓ **Recommendation 3.** Recommend the PCAOB, in consultation with auditors, investors, public companies, audit committees, boards of directors, academics, and others, determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.

**Recommendation 4.** Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit

committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.

(a) Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible. The AICPA and state boards of accountancy should clarify and prominently note that differences exist between the SEC and PCAOB standards (applicable to public companies) and the AICPA and state standards (applicable in all circumstances, but subject to SEC and PCAOB standards, in the case of public companies) and indicate, at each place in their standards where differences exist, that stricter SEC and PCAOB independence requirements applicable to public company auditors may supersede or supplement the stated requirements. This compilation should not require rulemaking by either the SEC or the PCAOB because it only calls for assembly and compilation of existing rules.

(b) Develop training materials to help foster and maintain the application of healthy professional skepticism with respect to issues of independence and other conflicts among public company auditors, and inspect auditing firms, through the PCAOB inspection process, for independence training of partners and mid-career professionals.

**Recommendation 5.** Adopt annual shareholder ratification of public company auditors by all public companies.

**Recommendation 6.** Enhance regulatory collaboration and coordination between the PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the United States.



**2**

**American Institute of  
Certified Public  
Accountants**



Barry C. Melancon, CPA, CGMA  
President and CEO  
American Institute of CPAs  
1211 Avenue of the Americas  
New York, NY 10036-8775

September 27, 2016

Dr. Parveen Gupta  
Lynn E. Turner  
Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory Committee on the Auditing Profession

Dear Dr. Gupta and Mr. Turner:

As requested in your letter dated June 27, it is my pleasure to provide an update of activities undertaken by the American Institute of Certified Public Accountants (AICPA) in relation to the recommendations of the Advisory Committee on the Auditing Profession (ACAP). The AICPA is committed to advancing auditing in the future and building a culture on campuses and within firms that attracts, develops and retains the best and brightest talent. We have had significant success achieving the outcomes envisioned by the ACAP recommendations.

Below is a summary of those efforts.

#### **Human Capital Recommendations**

***Recommendation 1. Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high-quality audits.***

- In 2014, we launched a practice analysis – a comprehensive research project to identify the knowledge and skills required of newly licensed CPAs so that they are ready to meet current and future needs of the auditing profession. This insight informed the next version of the Uniform CPA Examination (the Exam) that launches in April 2017. Further, we are implementing a recurring practice analysis process that will continue to evolve the Exam to remain relevant and aligned with the evolving needs of the public interest.
- Also in 2014, the AICPA launched a website and newsletter, Extra Credit, for educators. The website includes lesson plans and other resources to help teachers integrate accounting curricula aligned with the evolving skills needed for effective auditing into their classrooms. The newsletter curates stories, ideas and innovation related to accounting education.
- We recently added a section to our student site, StartHereGoPlaces.org, that includes content from the Center for Audit Quality's *Discover Audit* campaign.

***Recommendation 2. Improve the representation and retention of minorities in the auditing profession so as to enrich the pool of human capital in the profession.***

- In 2012, we established the AICPA National Commission on Diversity and Inclusion to develop strategies to recruit, retain and advance under-represented minorities and invited leaders from the diversity-specific organizations to be part of the Commission whose goal is to increase minority participation and inclusion in all size auditing firms.
- The AICPA Fellowship for Minority Doctoral Students focuses on increasing the number of minority CPAs who serve as role models and mentors in the classroom. The program has provided funding for more than 150 minority doctoral candidates since its inception.
- This fall we are launching several initiatives to attract minorities to the profession. They include a national awareness campaign; and a recognition program for high school students and a pilot program at select universities, including HBCU/HCI institutions, to provide influential faculty with resources to move students through to the CPA exam.

**Recommendation 3. *Ensure the sufficiently robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high-quality audits.***

- The AICPA Foundation created the Accounting Doctoral Scholars (ADS) program in 2008 to increase the supply of Ph.Ds. in accounting concentrating on audit or tax. The Foundation raised more than \$17 million to fund practical experienced PhDs. To date, 108 participants have benefited from the ADS program and 69 of them have joined university faculties. The remaining scholars will complete their doctoral studies by the end of 2017. A new iteration of the ADS program launched in August 2016.

**Recommendation 5. *Encourage the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association (AAA) jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession.***

- In 2012 the AAA and AICPA formed the Pathways Commission on Accounting Higher Education, bringing together more than 100 volunteers from practice and academia in an unprecedented effort. Many programs and initiatives were created from this work and the AICPA and AAA continue to collaborate on Pathways-inspired initiatives. A key deliverable was a standard change by the largest accrediting body to allow for more recognition of practical experience in the classroom.
- A signature recommendation of the Pathways Commission was the development of a high school accounting course that is eligible for Advanced Placement (AP) credit. A course was submitted to the College Board. While the College Board is not approving any new courses at this time, a decision was made by the AICPA to support and grow an advanced high school accounting course through other avenues.

### **Concentration and Competition Recommendations**

**Recommendation 4. *Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.***

Through the AICPA Professional Ethics Executive Committee (PEEC), the AICPA devotes significant resources to independence and ethics activities. PEEC has developed many initiatives and resources in recent years related to this recommendation, including:

- Revising the AICPA Code of Professional Conduct (AICPA Code) so CPAs can more easily apply the rules and reach correct conclusions.
- Developing the AICPA Plain English Guide to Independence to assist CPAs in understanding independence requirements.
- Maintaining an up-to-date comparison of AICPA and SEC independence requirements, in addition to comparisons of the AICPA rules with those of the GAO and DOL.
- In addition, the AICPA has produced several behavioral and regulatory ethics courses that explore the distinctive ethical code of the profession.

Beyond these activities, through efforts of its Peer Review Program and the Assurance Services Executive Committee (ASEC), the AICPA is driving additional activities to promote excellence in audit across the profession.

The AICPA has launched the Enhancing Audit Quality initiative, a comprehensive effort to consider auditing of private entities through multiple touch points, particularly where quality issues have emerged. Simultaneously, the ASEC and the Auditing Standards Board (ASB) are collaborating on activities to advance auditing in the future and open doors to transform the traditional financial statement audit. Audit innovation will require enhanced analytical skills, and CPAs are also increasingly bringing their core competency in assurance to new subject matter areas such as information security, where IT audit skills are of paramount importance. We are committed to and excited about the opportunities for CPAs to understand and engage in auditing in the future.

Sincerely,

AICPA



Barry C. Melancon, CPA, CGMA  
AICPA President and CEO



Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession

June 27, 2016

Barry C. Melancon  
President and Chief Executive Officer  
American Institute of Certified  
Public Accountants  
1211 Avenue of the Americas  
New York, New York 10036-8775

Dear President Melancon:

In 2007 the U.S. Secretary of the Treasury, the Honorable Henry M. Paulson, Jr., announced and appointed an Advisory Committee on the Auditing Profession (ACAP) "...to consider and develop recommendations relating to the sustainability of the auditing profession." Secretary Paulson appointed twenty one members to the Committee, including you. The members of the committee had a variety of backgrounds including business executives and corporate board members, former Securities and Exchange Commission (SEC) and Federal Reserve Chairmen, former SEC chief accountants, auditors, investors and attorneys. As you are aware, a year later in October 2008, the ACAP issued its recommendations.

The PCAOB Investor Advisory Group (IAG) meets annually with the PCAOB board members and staff to discuss issues important to investors, the PCAOB and auditing profession. We again look forward to our next meeting on October 27, 2016. At that meeting, a working group of the IAG will be making a presentation to the members of the PCAOB with respect to the progress that has been made in the intervening eight years, on the recommendations of the ACAP. Accordingly, the working group is diligently undertaking to identify the actions taken to date by each entity to which the recommendations were addressed, as well as what obstacles, if any, they have faced in addressing the ACAP recommendations.

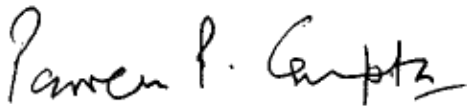
To that end, the working group would appreciate it if the PCAOB or its staff, could provide a response to the working group, with respect to the ACAP recommendations to the PCAOB in the attached Appendix A, which have been highlighted. (A similar request is being sent to each entity that the ACAP directed its recommendations to.) In particular, if the response could set forth the steps or actions taken to address and implement the recommendations, and when they were taken, would be most useful. This would include either interim or final actions. Such a response would be helpful in ensuring our report to the PCAOB is as comprehensive as possible. In order to adequately consider the response, it would be appreciated if it could be received by no later than September 15, 2016. You

can address it to the working group co-chair. Parveen Gupta, Lehigh University, 621 Taylor Street, College of Business and Economics, Lehigh University, Bethlehem PA, 18015. Please do not hesitate to Call Mr. Gupta (610-758-3443) or Mr. Turner (303-956-4895) if you have any questions.

This project is being undertaken by the IAG working group and its members. As such, it is not a project being undertaken by the PCAOB or its staff. However, we hope it will result in a report that is informative and helpful to the PCAOB in its endeavors.

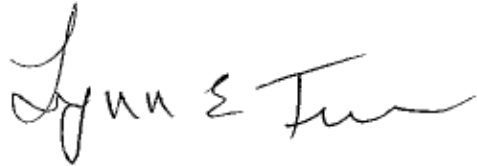
Again, we greatly appreciate your support.

Sincerely,



Parveen Gupta

Investor Advisory Group  
Working Committee Co-Chair



Lynn E. Turner

Investor Advisory Group  
Working Committee Co-Chair

## APPENDIX A

### U.S. Treasury Advisory Committee on the Auditing Profession

October, 2008 Report

Recommendations made to the Securities and Exchange Commission and Others

### Advisory Committee on the Auditing Profession Final Report

#### Human Capital Recommendations

- ✓ **Recommendation 1.** Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high quality audits.
  - ✓ (a) Regularly update the accounting certification examinations to reflect changes in the accounting profession, its relevant professional and ethical standards, and the skills and knowledge required to serve increasingly global capital markets.
  - ✓ (b) Reflect real world changes in the business environment more rapidly in teaching materials.
  - ✓ (c) Require that schools build into accounting curricula current market developments.
- ✓ **Recommendation 2.** Improve the representation and retention of minorities in the auditing profession so as to enrich the pool of human capital in the profession.
  - ✓ (a) Recruit minorities into the auditing profession from other disciplines and careers.
  - ✓ (b) Institute initiatives to increase the retention of minorities in the profession.
  - ✓ (c) Emphasize the role of community colleges in the recruitment of minorities into the auditing profession.
  - ✓ (d) Emphasize the utility and effectiveness of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.
  - ✓ (e) Increase the numbers of minority accounting doctorates through focused efforts.

✓ **Recommendation 3.** Ensure a sufficiently robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high quality audits.

✓ (a) Increase the supply of accounting faculty through public and private funding and raise the number of professionally qualified faculty that teach on campuses.

✓ (b) Emphasize the utility and effectiveness of cross-sabbaticals.

✓ (c) Create a variety of tangible and sufficiently attractive incentives that will motivate private sector institutions to fund both accounting faculty and faculty research, to provide practice materials for academic research and for participation of professionals in behavioral and field study projects, and to encourage practicing accountants to pursue careers as academically and professionally qualified faculty.

**Recommendation 4.** Develop and maintain consistent demographic and higher education program profile data.

✓ **Recommendation 5.** Encourage the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession.

### **Firm Structure and Finances Recommendations**

**Recommendation 1.** Urge the Securities and Exchange Commission (SEC), and Congress as appropriate, to provide for the creation by the Public Company Accounting Oversight Board (PCAOB) of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.

**Recommendation 2.** Encourage greater regulatory cooperation and oversight of the public company auditing profession to improve the quality of the audit process and enhance confidence in the auditing profession and financial reporting.



(a) Institute the following mechanism to encourage the states to substantially adopt the mobility provisions of the Uniform Accountancy Act, Fifth Edition (UAA): If states have failed to adopt the mobility provisions of the UAA by December 31, 2010, Congress should pass a federal provision requiring those states to adopt these provisions.

(b) Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.

(c) Urge the states to create greater financial and operational independence of their state boards of accountancy.

**Recommendation 3.** Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze, explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.

**Recommendation 4.** Urge the SEC to amend Form 8-K disclosure requirements to characterize appropriately and report every public company auditor change and to require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audit clients.

**Recommendation 5.** Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor's standard reporting model. Further, urge that the PCAOB and the SEC clarify in the auditor's report the auditor's role in detecting fraud under current auditing standards and further that the PCAOB periodically review and update these standards.

**Recommendation 6.** Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report.

**Recommendation 7.** Urge the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating (a) information required by the EU's Eighth Directive, Article 40 Transparency Report deemed appropriate by the PCAOB, and (b) such key indicators of audit quality and effectiveness as determined by the PCAOB in accordance with Recommendation 3 in Chapter VIII [Concentration and Competition] of this Report. Further, urge the PCAOB to require that, beginning in 2011, the larger auditing firms file with the PCAOB on a confidential basis audited financial statements.

## **Concentration and Competition Recommendations**

**Recommendation 1.** Reduce barriers to the growth of smaller auditing firms consistent with an overall policy goal of promoting audit quality. Because smaller auditing firms are likely to become significant competitors in the market for larger company audits only in the long term, the Committee recognizes that Recommendation 2 will be a higher priority in the near term.

(a) Require disclosure by public companies in their registration statements, annual reports, and proxy statements of any provisions in agreements with third parties that limit auditor choice.

✓ (b) Include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements.

**Recommendation 2.** Monitor potential sources of catastrophic risk faced by public company auditing firms and create a mechanism for the preservation and rehabilitation of troubled larger public company auditing firms.

(a) As part of its current oversight over registered auditing firms, the PCAOB should monitor potential sources of catastrophic risk which would threaten audit quality.

(b) Establish a mechanism to assist in the preservation and rehabilitation of a troubled larger auditing firm. A first step would encourage larger auditing firms to adopt voluntarily a contingent streamlined internal governance mechanism that could be triggered in the event of threatening circumstances. If the governance mechanism failed to stabilize the firm, a second step would permit the SEC to appoint a court-approved trustee to seek to preserve and rehabilitate the firm by addressing the threatening situation, including through a reorganization, or if such a step were unsuccessful; to pursue an orderly transition.

**Recommendation 3.** Recommend the PCAOB, in consultation with auditors, investors, public companies, audit committees, boards of directors, academics, and others, determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.

✓ **Recommendation 4.** Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit

committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.

- ✓ (a) Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible. The AICPA and state boards of accountancy should clarify and prominently note that differences exist between the SEC and PCAOB standards (applicable to public companies) and the AICPA and state standards (applicable in all circumstances, but subject to SEC and PCAOB standards, in the case of public companies) and indicate, at each place in their standards where differences exist, that stricter SEC and PCAOB independence requirements applicable to public company auditors may supersede or supplement the stated requirements. This compilation should not require rulemaking by either the SEC or the PCAOB because it only calls for assembly and compilation of existing rules.
- ✓ (b) Develop training materials to help foster and maintain the application of healthy professional skepticism with respect to issues of independence and other conflicts among public company auditors, and inspect auditing firms, through the PCAOB inspection process, for independence training of partners and mid-career professionals.

**Recommendation 5.** Adopt annual shareholder ratification of public company auditors by all public companies.

**Recommendation 6.** Enhance regulatory collaboration and coordination between the PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the United States.

# 3

## **National Association of State Boards of Accountancy**



# NASBA

National Association of State Boards of Accountancy

150 Fourth Avenue North • Suite 700 • Nashville, TN 37219-2417 • Tel 615/880-4201 • Fax 615/880-4291 • kbishop@nasba.org

Ken L. Bishop  
President & CEO

September 12, 2016

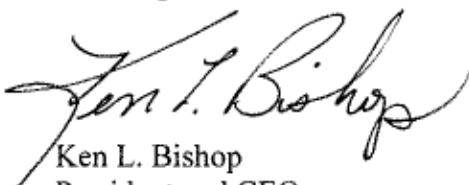
Parveen Gupta, Working Committee Co-Chair  
PCAOB Investor Advisory Group  
c/o Lehigh University  
College of Business and Economics  
621 Taylor Street  
Bethlehem, PA 18015

Dear Mr. Gupta:

Please find attached the responses from the National Association of State Boards of Accountancy (NASBA) to the recommendations made by the Advisory Committee on the Auditing Profession in their Final Report. NASBA has addressed the recommendations that were identified as having nexus to NASBA and State Boards of Accountancy.

NASBA remains committed to addressing the recommendations of the Final Report and strongly supports the PCAOB Investor Advisory Committee efforts. It is our intent to dedicate senior staff to continue implementation steps and the monitor and report on our progress. We appreciate the opportunity to participate and opine on these important recommendations.

Best Regards,



Ken L. Bishop  
President and CEO

Attachment

## **Human Capital Recommendations**

**Recommendation 1.** Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high quality audits.

- (a) Regularly update the accounting certification examinations to reflect changes in the accounting profession, its relevant profession and ethical standards, and the skills and knowledge required to serve increasingly global capital markets.

As a high stakes examination used as one requirement by the state boards of accountancy for professional licensing, the Uniform CPA Examination undergoes a rigorous periodic comprehensive research project called a practice analysis to ensure that it is adequately testing the knowledge and skills necessary to practice as a newly licensed CPA. This analysis includes large scale surveys of newly licensed CPAs and those who supervise them, as well as focus groups, to determine what skills and knowledge are needed. Input is also widely sought from interested parties including federal regulators such as the SEC and PCAOB, and the results of the practice analysis are exposed for public comment. In fact, representatives from both the SEC and PCAOB participated in advisory groups to the most recent practice analysis which just completed and published on April 2, 2016. As a result of this most recent practice analysis, significant updates to the CPA examination will launch on April 1, 2017 and include increased testing of higher order skills.

The AICPA Board of Examiners, made up of a majority of NASBA members, also has carefully followed policies and procedures to ensure that any new or revised standards, including those of the SEC and PCAOB, are tested in a stipulated timeframe after becoming effective. The item bank of test questions for the CPA examination are also continually reviewed for obsolescence, and such questions are purged as necessary.

- (b) Reflect real world changes in the business environment more rapidly in teaching materials.

Practice analysis activities, draft results and final results are all widely exposed to the public, including academia. Representatives of AAA and many educators are involved in the process, presentations are made at educator conferences nationwide and results are shared specifically with accounting educator organizations. To the extent that such educators follow changes in the content and skills tested in the CPA examination, it would follow that their teaching materials would be updated to include such content and skills. Beyond just accounting, auditing and tax topics, business law topics are included in the CPA examination, as is one complete section of the examination entitled Business Environment and Concepts. This section is part of the periodic practice analysis and, therefore, is reviewed extensively and updated on a timely basis.

Universities can also work with NASBA to obtain reports specific to their school which can give them greater insight into the content areas of the CPA examination on which their students perform better, worse or consistent with just passing candidates. This insight can be used as a tool to improve curricula and consider changes to teaching methods.

- (c) Require that schools build into curricula current market developments.

The state boards of accountancy do not require such specificity in their education requirements for licensing as a CPA, but do require certain minimum coverage in accounting, auditing and business coursework. Any market developments that would be deemed important to the knowledge and understanding of a newly licensed CPA through the extensive outreach during the periodic practice analysis would be incorporated into the content and skills of the next version of the CPA examination. At such time, it would be prudent for universities to include such topics in their curricula to afford their students a better opportunity to be successful in their efforts to pass the CPA examination.

## **Firm Structure and Finances Recommendations**

**Recommendation 2.** Encourage greater regulatory cooperation and oversight of the public company auditing profession to improve the quality of the audit process and enhance confidence in the auditing profession and financial reporting.

- (a) Institute the following mechanisms to encourage the state to substantially adopt the mobility provisions of the Uniform Accountancy Act, Fifth Edition (UAA). If states have failed to adopt the mobility provision requiring those state to adopt these provisions.

The individual mobility provisions of the Uniform Accountancy Act (now Seventh Edition of May 2014) (UAA) have been enacted by 49 of the 50 states, as well as multiple U.S. Territories. Mobility remains under consideration and discussion in Hawaii. Significant efforts were undertaken by NASBA and AICPA to work with the state boards of accountancy across the United States to pass this legislation. The current version of the UAA also has incorporated the concept of firm mobility to make such language available to states who wish to consider it. As of the date of this letter, 17 states allow for firm mobility.

- (b) Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.

Roundtable meetings are held at all NASBA meetings of the state boards of accountancy. Breakout sessions are conducted both regionally (all staff and board members) and separately for chairs of boards and executive directors of boards to discuss topics and trends of current interest, to share information and pose questions. These meetings are highly rated in the evaluations of our meetings as very important communication venues. A separate Executive Director and Legal Conference is also held each year which is specifically for



staff and legal counsel to state boards to gather and discuss matters of common interest.

NASBA's senior leadership meets with the PCAOB Board annually to discuss current projects and topics, and staff have ongoing dialogue. NASBA staff also have periodic meetings with the SEC, DOL and other federal agency representatives to discuss enforcement processes and efforts, and serve as a resource to both state boards and federal regulators for communication efforts. NASBA publishes a quarterly enforcement report for state boards which delineates all public enforcement actions taken against CPAs and CPA firms by federal agencies. It also provides an Enforcement Tools section on its website for state board use. This includes information about federal agency enforcement processes and how to obtain or share enforcement information with certain federal agencies.

Finally, while not a formal relationship, NASBA regularly invites leaders from Federal regulatory and enforcement agencies to speak at our regional and national conferences and meeting. This allows state regulators and enforcement officials to hear updates and changes that impact the accounting profession, and to opine or address questions to the presenters (as an example, James Doty, Chair of the Public Company Oversight Board, will be presenting at our annual meeting this fall).

- (c) Urge the state to create greater financial and operational independence of their state boards of accountancy.

NASBA added a Director of Governmental and Legislative Affairs position in 2012 and with it has substantially ramped up its capability to monitor any untoward legislation which could negatively impact the financial standing or operational independence of boards of accountancy. It has obtained legislation monitoring tools and works cooperatively with AICPA's state legislative team

in this effort. NASBA fully supports boards of accountancy when harmful legislation is introduced by providing testimony and written support, consultation and other measures.

**Recommendation 3.** Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze, explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm board and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.

There has been no direct action toward this recommendation, however, NASBA's Regulatory Response Committee assesses requests for comment issued by the PCAOB, the SEC and other state and federal accounting regulatory bodies in an effort to enhance the public protection mandate afforded Boards of Accountancy.

### **Concentration and Competition Recommendations**

**Recommendation 4.** Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.

- (a) Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible. The AICPA and state boards of accountancy should clarify and prominently note that differences exist between SEC and PCAOB standards (applicable to public companies) and indicate, at each place in their standards where differences exist, that stricter SEC and PCAOB independence requirements applicable to public company auditors may supersede or supplement the stated requirements. This

compilation should not require rulemaking by either the SEC or PCAOB because it only calls for assembly and compilation of existing rules.

AICPA publically provides a document entitled *AICPA Plain English Guide to Independence* which clearly delineates basic differences between the AICPA Code of Conduct and the SEC and PCAOB independence rules and standards. This document is updated annually and available on its website. State board of accountancy statutes and rules specifically require compliance with PCAOB standards and provides for enforcement rights when such standards are not followed or enforcement actions are taken by SEC or PCAOB.

NASBA and most states' Boards of Accountancy have web sites that include links to the jurisdictions laws and rules, including the jurisdictions Code of Conduct/Ethics. Many Boards have adopted the AICPA Code of Conduct (Code) by reference and others have adopted the AICPA Code of Conduct with some exceptions. If the Code is adopted with exception, the Board lists exceptions to the Code in its rules.

- (b) Develop training materials to help foster and maintain the application of healthy professional skepticism with respect to issues of independence and other conflicts among public company auditors, and inspect auditing firms, through the PCAOB inspection process, for independence training of partners and mid-career professionals.

AICPA is in the midst of several projects focused on enhancing audit quality and the future of practice monitoring. NASBA State Board volunteers serve on most of the AICPA committees and Task Forces involved in these projects. NASBA, on behalf of Boards of Accountancy, is also actively monitoring these projects, providing feedback to the AICPA and information to Boards of

Accountancy through various outlets, including monthly newsletters and regional and annual conferences.

NASBA's wholly owned subsidiary, the NASBA Center for Public Trust's mission is to champion the public trust by advancing ethical leadership in business, institutions and organizations. It provides periodic training on ethics matters and also sponsors Student Center for Public Trust chapters on university campuses across the nation. As part of its training program, it has sponsored Center for Audit Quality case study sessions on professional skepticism, conflicts of interest and independence topics.



Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession

June 27, 2016

Ken L. Bishop  
President and Chief Executive Officer  
National Association of State  
Boards of Accountancy  
150 Fourth Ave. North, Ste. 700  
Nashville, TN 37219-2417

Dear: President Bishop:

In 2007 the U.S. Secretary of the Treasury, the Honorable Henry M. Paulson, Jr., announced and appointed an Advisory Committee on the Auditing Profession (ACAP) "...to consider and develop recommendations relating to the sustainability of the auditing profession." Secretary Paulson appointed twenty one members to the Committee, with a variety of backgrounds including business executives and corporate board members, former Securities and Exchange Commission (SEC) and Federal Reserve Chairmen, former SEC chief accountants, auditors, investors and attorneys. Gaylen Hansen, an active member in NASBA was a member of the Committee. A year later in October 2008, the ACAP issued its recommendations.

The PCAOB Investor Advisory Group (IAG) has benefited, as we hope the PCAOB board members and staff have, from the discussions at the IAG meetings in past years. We again look forward to our next meeting on October 27, 2016. At that meeting, a working group of the IAG will be making a presentation to the members of the PCAOB with respect to the progress that has been made in the intervening eight years, on the recommendations of the ACAP. Accordingly, the working group is diligently undertaking to identify the actions taken to date by each entity to which the recommendations were addressed, as well as what obstacles, if any, they have faced in addressing the ACAP recommendations.

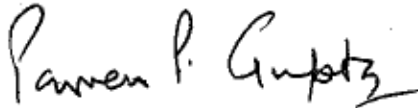
To that end, the working group would appreciate it if NASBA or its staff, could provide a response to the working group, with respect to the ACAP recommendations to NASBA in the attached Appendix A, which have been highlighted. (A similar request is being sent to each entity that the ACAP directed its recommendations to.) In particular, if the response could set forth the steps or actions taken to address and implement the recommendations, and when they were taken, would be most useful. This would include either interim or final actions. Such a response would be helpful in ensuring our report to the PCAOB is as comprehensive as possible. In order to adequately consider the response, it would be appreciated if it could be received by no later than September 15, 2016. You can address it to the working group co-chair. Parveen

Gupta, Lehigh University, 621 Taylor Street, College of Business and Economics, Lehigh University, Bethlehem PA, 18015. Please do not hesitate to Call Mr. Gupta (610-758-3443) or Mr. Turner (303-956-4895) if you have any questions.

This project is being undertaken by the IAG working group and its members. As such, it is not a project being undertaken by the PCAOB or its staff. However, we hope it will result in a report that is informative and helpful to the PCAOB in its endeavors.

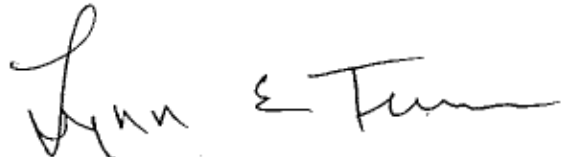
Again, we greatly appreciate your support.

Sincerely,



Parveen Gupta

Investor Advisory Group  
Working Committee Co-Chair



Lynn E. Turner

Investor Advisory Group  
Working Committee Co-Chair

## APPENDIX A

### U.S. Treasury Advisory Committee on the Auditing Profession

October, 2008 Report

Recommendations made to the Securities and Exchange Commission and Others

### Advisory Committee on the Auditing Profession Final Report

#### Human Capital Recommendations

- ✓ **Recommendation 1.** Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high quality audits.
  - ✓ (a) Regularly update the accounting certification examinations to reflect changes in the accounting profession, its relevant professional and ethical standards, and the skills and knowledge required to serve increasingly global capital markets.
  - ✓ (b) Reflect real world changes in the business environment more rapidly in teaching materials.
  - ✓ (c) Require that schools build into accounting curricula current market developments.
  
- Recommendation 2.** Improve the representation and retention of minorities in the auditing profession so as to enrich the pool of human capital in the profession.
  - (a) Recruit minorities into the auditing profession from other disciplines and careers.
  - (b) Institute initiatives to increase the retention of minorities in the profession.
  - (c) Emphasize the role of community colleges in the recruitment of minorities into the auditing profession.
  - (d) Emphasize the utility and effectiveness of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.
  - (e) Increase the numbers of minority accounting doctorates through focused efforts.

**Recommendation 3.** Ensure a sufficiently robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high quality audits.

(a) Increase the supply of accounting faculty through public and private funding and raise the number of professionally qualified faculty that teach on campuses.

(b) Emphasize the utility and effectiveness of cross-sabbaticals.

(c) Create a variety of tangible and sufficiently attractive incentives that will motivate private sector institutions to fund both accounting faculty and faculty research, to provide practice materials for academic research and for participation of professionals in behavioral and field study projects, and to encourage practicing accountants to pursue careers as academically and professionally qualified faculty.

**Recommendation 4.** Develop and maintain consistent demographic and higher education program profile data.

**Recommendation 5.** Encourage the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession.

#### **Firm Structure and Finances Recommendations**

**Recommendation 1.** Urge the Securities and Exchange Commission (SEC), and Congress as appropriate, to provide for the creation by the Public Company Accounting Oversight Board (PCAOB) of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.

✓ **Recommendation 2.** Encourage greater regulatory cooperation and oversight of the public company auditing profession to improve the quality of the audit process and enhance confidence in the auditing profession and financial reporting.

- ✓ (a) Institute the following mechanism to encourage the states to substantially adopt the mobility provisions of the Uniform Accountancy Act, Fifth Edition (UAA): If states have failed to adopt the mobility provisions of the UAA by December 31, 2010, Congress should pass a federal provision requiring those states to adopt these provisions.
  - ✓ (b) Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.
  - ✓ (c) Urge the states to create greater financial and operational independence of their state boards of accountancy.
- ✓ **Recommendation 3.** Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze, explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.

**Recommendation 4.** Urge the SEC to amend Form 8-K disclosure requirements to characterize appropriately and report every public company auditor change and to require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audit clients.

**Recommendation 5.** Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor's standard reporting model. Further, urge that the PCAOB and the SEC clarify in the auditor's report the auditor's role in detecting fraud under current auditing standards and further that the PCAOB periodically review and update these standards.

**Recommendation 6.** Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report.

**Recommendation 7.** Urge the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating (a) information required by the EU's Eighth Directive, Article 40 Transparency Report deemed appropriate by the PCAOB, and (b) such key indicators of audit quality and effectiveness as determined by the PCAOB in accordance with Recommendation 3 in Chapter VIII [Concentration and Competition] of this Report. Further, urge the PCAOB to require that, beginning in 2011, the larger auditing firms file with the PCAOB on a confidential basis audited financial statements.



## **Concentration and Competition Recommendations**

**Recommendation 1.** Reduce barriers to the growth of smaller auditing firms consistent with an overall policy goal of promoting audit quality. Because smaller auditing firms are likely to become significant competitors in the market for larger company audits only in the long term, the Committee recognizes that Recommendation 2 will be a higher priority in the near term.

(a) Require disclosure by public companies in their registration statements, annual reports, and proxy statements of any provisions in agreements with third parties that limit auditor choice.

(b) Include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements.

**Recommendation 2.** Monitor potential sources of catastrophic risk faced by public company auditing firms and create a mechanism for the preservation and rehabilitation of troubled larger public company auditing firms.

(a) As part of its current oversight over registered auditing firms, the PCAOB should monitor potential sources of catastrophic risk which would threaten audit quality.

(b) Establish a mechanism to assist in the preservation and rehabilitation of a troubled larger auditing firm. A first step would encourage larger auditing firms to adopt voluntarily a contingent streamlined internal governance mechanism that could be triggered in the event of threatening circumstances. If the governance mechanism failed to stabilize the firm, a second step would permit the SEC to appoint a court-approved trustee to seek to preserve and rehabilitate the firm by addressing the threatening situation, including through a reorganization, or if such a step were unsuccessful, to pursue an orderly transition.

**Recommendation 3.** Recommend the PCAOB, in consultation with auditors, investors, public companies, audit committees, boards of directors, academics, and others, determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.

✓ **Recommendation 4.** Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit

committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.

- ✓ (a) Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible. The AICPA and state boards of accountancy should clarify and prominently note that differences exist between the SEC and PCAOB standards (applicable to public companies) and the AICPA and state standards (applicable in all circumstances, but subject to SEC and PCAOB standards, in the case of public companies) and indicate, at each place in their standards where differences exist, that stricter SEC and PCAOB independence requirements applicable to public company auditors may supersede or supplement the stated requirements. This compilation should not require rulemaking by either the SEC or the PCAOB because it only calls for assembly and compilation of existing rules.
- ✓ (b) Develop training materials to help foster and maintain the application of healthy professional skepticism with respect to issues of independence and other conflicts among public company auditors, and inspect auditing firms, through the PCAOB inspection process, for independence training of partners and mid-career professionals.

**Recommendation 5.** Adopt annual shareholder ratification of public company auditors by all public companies.

**Recommendation 6.** Enhance regulatory collaboration and coordination between the PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the United States.

# 4

## **Public Company Accounting Oversight Board**

# PCAOB

Public Company Accounting Oversight Board

1666 K Street, N.W.  
Washington, DC 20006  
Telephone: (202) 207-9100  
Facsimile: (202) 862-8430  
[www.pcaobus.org](http://www.pcaobus.org)

September 16, 2016

Mr. Parveen Gupta  
Investor Advisory Group  
Co-Chair, Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession  
Lehigh University  
College of Business and Economics  
621 Taylor Street  
Bethlehem, PA 18015

Mr. Lynn Turner  
Investor Advisory Group  
Co-Chair, Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession

Dear Mr. Gupta and Mr. Turner,

Thank you for your letter dated June 27, 2016 and for your continued service on the Investor Advisory Group.

When the U.S. Treasury's 2008 Advisory Committee on the Auditing Profession (ACAP) recommendations were made, then Secretary Paulson noted their role in sustaining a robust auditing profession that encourages investor confidence in our financial market. The recommendations continue to be relevant in bettering audit quality and, thereby, improving investor confidence.

As you may know, the first update on our work in addressing the ACAP recommendations was provided at the October 2010 Standing Advisory Group meeting and is available on our website. Since then, Board members have provided updates directly to the IAG at their 2014 and 2013 meetings.

Recently, the PCAOB has taken significant action in two particular priority areas: transparency and the auditor reporting model. These actions address the recommendations to make the auditor's reporting model more useful to investors and to improve accountability and transparency. Specifically, the PCAOB has:

Mr. Parveen Gupta  
Mr. Lynn Turner  
September 16, 2016  
Page 2

1. Adopted final rules on December 15, 2015, *Rules to Require Disclosure of Certain Audit Participants on a new PCAOB form and Related Amendments to Auditing Standards* (PCAOB Release No. 2015-008, SEC approval May 9, 2016, see SEC Release No. 34-77787). These new rules and related amendments improve transparency regarding the engagement partner and other accounting firms that took part in the audit. The rules further require disclosure of the name of the engagement partner and information about other accounting firms.
2. Proposed the *Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion and Related Amendments to PCAOB Standards* on May 11, 2016 (PCAOB Release No. 2016-003). This re-proposal, among other things, requires auditors to report "critical audit matters" specific to each audit. In this way, the proposed requirement would provide audit specific information about especially challenging, subjective, or complex aspects of the audit as they relate to the relevant financial statement accounts and disclosures.

In order to be as responsive as possible to your request, I've attached at Tab 1 a summary chart assembled by PCAOB staff of the steps taken to address the specific ACAP recommendations that you highlighted in your letter. For further information on actions taken for all ACAP recommendations and background on the recommendations, included at Tab 2 is Board Member Franzel's April 2016 article. The Board's 2010 publication is also included for background at Tab 3.

I hope that the attached information provides you with the information you need. Please do not hesitate to contact me should you need any further information or have any questions.

Again, I greatly appreciate your continued participation on the IAG and your leadership on this working group.

Sincerely,



James R. Doty  
Chairman



**Appendix A: Summary of actions taken responsive to the ACAP recommendations highlighted by the IAG working group**

The table below summarizes initiatives that address or begin to address the ACAP recommendations highlighted in the June 27, 2016 letter from the IAG working group.<sup>1</sup>

<b>ACAP Recommendation (excerpt)</b>	<b>Summary of initiatives</b>	<b>Current Status</b>
<p><b>Rec. 1:</b> Urge the SEC and Congress, as appropriate, to provide for the creation by the PCAOB of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.</p>	<ul style="list-style-type: none"> <li>• PCAOB Center for Economic Analysis (CEA) has two specific initiatives relating to fraud:                             <ul style="list-style-type: none"> <li>○ <i>Fraud case studies:</i> An initiative to analyze specific instances of fraud to better understand and identify commonalities across cases (including, for example, 'red flags') as well as actions that could have uncovered the fraud. The cases seek to shed light on how the fraud developed over time, highlight economic impacts of the fraud, and identify key 'takeaways' based on a detailed analysis of the audit work performed. These studies support internal training and are intended to have other uses.</li> <li>○ <i>Fraud database:</i> An initiative to make better data on financial statement fraud available to the public. One goal is to encourage academics/researchers to explore issues related to accounting fraud and that can inform PCAOB oversight. In addition, the fraud database expects to provide the PCAOB with:                                     <ul style="list-style-type: none"> <li>▪ Access to information used in the development of economic analysis in standard setting;</li> <li>▪ An enhanced understanding of how standards might address problems in practice;</li> <li>▪ An ability to analyze robust data that may, among other things, inform the PCAOB's risk assessments; and</li> <li>▪ Support for fulfilling the investor protection mandate by a continuing focus and structured analysis of fraud.</li> </ul> </li> </ul> </li> </ul>	<p>Ongoing consideration.</p>
<p><b>Rec. 2(b):</b> Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.</p>	<ul style="list-style-type: none"> <li>• The staff coordinates and meets regularly with various regulators to discuss respective oversight responsibilities, including quarterly meetings among FASB, SEC and PCAOB as well as meeting with IAASB, AICPA, GAO, IFIAR, DOL, FinRA, and U.S. Federal Financial Regulatory Agencies.</li> </ul>	<p>Ongoing practice.</p>

<sup>1</sup> This table has been assembled by PCAOB staff and does not necessarily reflect the view of the Board or of other Board members or staff.

**Appendix A: Summary of actions taken responsive to the ACAP recommendations highlighted by the IAG working group**

<b>ACAP Recommendation (excerpt)</b>	<b>Summary of initiatives</b>	<b>Current Status</b>
<p><b>Rec.3:</b> Urge the PCAOB and the SEC, in consultation with other[s] . . . , to analyze, explore and enable , as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.</p>	<ul style="list-style-type: none"> <li>As part of regular oversight, engage in dialogues with largest firms regarding firm governance practices, among other things.</li> </ul>	<p>Ongoing practice.</p>
<p><b>Rec.4:</b> Urge the SEC to amend form 8-K disclosure requirements to characterize appropriately and report every public company auditor change and require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audit clients.</p>	<ul style="list-style-type: none"> <li>2011 – Discussions at November SAG meeting regarding disclosure of audit partners and initial rule proposal.</li> <li>2013 - Standards regarding disclosure of participants in an audit re-proposed.</li> <li>2015 – Supplemental request for comment issued.</li> <li>December 2015 – Board adopted final standard requiring the public disclosure of the name of the engagement partner on each completed audit, noting “The disclosures . . . will reveal engagement partner rotations to investors, including instances where engagement partners left the engagement before rotation would have been required.”</li> <li>Through ongoing inspection, PCAOB monitors staffing of audit engagements.</li> </ul>	<p>Final rule.</p>
<p><b>Rec. 5:</b> Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor’s standard reporting model. Further, urge that the PCAOB and the SEC clarify in the auditor’s report the auditor’s role in detecting fraud under current auditing standards and further that the PCAOB periodically review and update these standards.</p>	<ul style="list-style-type: none"> <li>2011 – PCAOB issued a concept release with the objective being to discuss several alternatives for changing the auditor’s reporting model that could increase its transparency and relevance of the financial statement users. Concept release followed by roundtable discussions and discussion at 2011 and 2012 SAG meetings.</li> <li>2013 – PCAOB proposed auditor reporting standard that would require the auditor to communicate in the auditor’s report “critical audit matters” specific to each audit (PCAOB Release 2013-005). The proposal also added the phrase “whether due to error or fraud” in the auditor’s report when describing the auditor’s responsibilities under the PCAOB standards to obtain reasonable assurance about whether the financial statements are free of material misstatements.</li> <li>May 2016 – Standards re-proposed. The re-proposal included critical audit matters that would inform investors and other financial statement users of matters arising from the audit that required especially challenging, subjective, or complex aspects of the audit as they relate to the relevant financial statement accounts and disclosures. (PCAOB Release 2016-003).</li> <li>2016- Re-proposal discussed with SAG; planned IAG discussion.</li> </ul>	<p>Standard re-proposed, comments period closed on August 15, 2016.</p>
<p><b>Rec 6:</b> Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner’s</p>	<ul style="list-style-type: none"> <li>2009 – Concept release regarding a standard to require engagement partner to sign audit report</li> </ul>	<p>Final Rule.</p>

Appendix A: Summary of actions taken responsive to the ACAP recommendations highlighted by the IAG working group

ACAP Recommendation (excerpt)	Summary of initiatives	Current Status
<p>signature on the auditor's report.</p>	<ul style="list-style-type: none"> <li>• 2011 – Board proposed standard requiring disclosure of the engagement partner's name in the auditor's report.</li> <li>• 2011 – Discussions at November SAG meeting.</li> <li>• 2013 - Standards re-proposed.</li> <li>• 2015 – Supplemental request for comment issued to solicit comment on disclosure of name of the engagement partner and information about certain other participants in the audit on a new PCAOB form, Form AP, <i>Auditor Reporting of Certain Audit Participants</i> ("Form AP").</li> <li>• December 2015 – Board adopted final rules requiring the public disclosure of the name of the engagement partner and other accounting firms participating in the audit on Form AP for each completed audit on new form AP and did not adopt a signature requirement.</li> </ul>	
<p><b>Rec 7:</b> Urge the PCAOB to require that . . . larger auditing firms produce a public annual report incorporating (a) information required by the EU's Eighth Directive, Article 40 Transparency report. . . and (b) such key indicators of audit quality and effectiveness as determined by the PCAOB in accordance with Recommendation 3 in Chapter VIII of this report. Further, urge the PCAOB to require that . . . the larger auditing firms file with the PCAOB on a confidential basis audited financial statements.</p>	<ul style="list-style-type: none"> <li>• 2013 – IAG and SAG discussions on Audit Quality Indicators.</li> <li>• 2014 &amp; 2015 – Continued discussions with SAG on Audit Quality Indicators; presentation on Audit Quality Indicators at IFIAR.</li> <li>• 2015 – Concept release issued on Audit Quality Indicators.</li> <li>• 2015 – Discussion with SAG of comments on Concept Release and possible next steps on AQIs.</li> <li>• Comments on concept released analyzed; planning for ways to continue to study AQIs, and to encourage their voluntary use.</li> </ul>	<p>Concept release, comment period closed.</p>

Appendix A: Summary of actions taken responsive to the ACAP recommendations highlighted by the IAG working group

ACAP Recommendation (excerpt)	Summary of initiatives	Current Status
<p><b>Rec.1(b):</b> Include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements.</p>	<ul style="list-style-type: none"> <li>• PCAOB includes representatives from smaller firms on its SAG and in public meetings and conducts outreach to smaller auditing firms as well as firms that audit broker dealers.</li> </ul>	
<p><b>Rec. 2, 2(a), 2(b):</b> Monitor potential sources of catastrophic risk . . . and create a mechanism for the preservation and rehabilitation of troubled larger public company auditing firms. (a) [T]he PCAOB should monitor potential sources of catastrophic risk which would threaten audit quality. (b) Establish a mechanism to assist in the preservation and rehabilitation of a troubled larger auditing firm [including encouraging] larger auditing firms to adopt voluntarily a contingent streamlined internal governance mechanism that could be triggered in the event of threatening circumstances. . . .</p> <p><b>Rec 3:</b> Recommend the PCAOB, in consultation with [others], determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.</p>	<ul style="list-style-type: none"> <li>• 2014 – 2014-2018 Strategic Plan highlights monitoring of and analyzing business models with a focus on identifying and responding to potential audit quality risks posed by such business models.</li> <li>• As part of regular oversight, engage in dialogues with firms about current events that may affect their business or auditor practice.</li> </ul>	<p>Ongoing practice.</p>
<p><b>Rec 4, 4(a) and 4(b):</b> Promote the understanding of and compliance with auditor independence requirements . . . in order to enhance investor confidence in the quality of the audit process and audits. 4(a) Compile SEC and PCAOB independence requirements into a single document and make this document website accessible. . . ; 4(b) Develop training materials to help foster and maintain the application of healthy professional skepticism. . .</p>	<ul style="list-style-type: none"> <li>• 2013 – IAG and SAG discussions on Audit Quality Indicators.</li> <li>• 2014 &amp; 2015 – Continued discussions with SAG on Audit Quality Indicators; presentation on Audit Quality Indicators at IFIAR.</li> <li>• 2015 – Concept release issued on Audit Quality Indicators.</li> <li>• 2015 – Discussion with SAG of comments on Concept Release and possible next steps on AQIs.</li> <li>• Comments on concept release analyzed; planning for ways to continue to study AQIs, and to encourage their voluntary use.</li> </ul>	<p>Concept release, comment period closed.</p>
<p><b>Concentration and competition recommendations</b></p>	<ul style="list-style-type: none"> <li>• Enforcement and Inspections (ongoing) PCAOB settled disciplinary orders for auditor independence violations with several audit firms, most recently in September 2016; DRI continues to monitor for compliance with independence requirements.</li> <li>• 2012 – Staff Audit Practice Alert No. 10 published on <i>Maintaining and Applying Professional Skepticism in Audits</i>.</li> <li>• 2011 – PCAOB launched the Forum for Auditors of Broker-Dealers. To promote accessibility, this forum has been held in various US locations, is offered at no cost and provides an opportunity for auditors of brokers or dealers to learn about and discuss PCAOB issues by attending seminars, webinars and discussions with PCAOB staff and Board members.</li> <li>• 2004 - PCAOB launched the Forum on Auditing in the Small Business Environment, a program for representatives of the small business community to learn more about PCAOB work and the impact of new auditing standards. To promote accessibility, forum has been held in various US locations, is offered at no cost, and provides an opportunity for</li> </ul>	<p>Ongoing practice.</p>

**Appendix A: Summary of actions taken responsive to the ACAP recommendations highlighted by the IAG working group**

<b>ACAP Recommendation (excerpt)</b>	<b>Summary of initiatives</b>	<b>Current Status</b>
<p><b>Rec 6:</b> Enhance regulatory collaboration and coordination between PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the United States.</p>	<p>auditors from smaller registered public accounting firms to learn about and discuss PCAOB issues by attending seminars, webinars and discussions with PCAOB staff and Board members.</p> <ul style="list-style-type: none"> <li>• PCAOB continues efforts to collaborate through:               <ul style="list-style-type: none"> <li>○ International inspections (as of September 2015, in 45 countries).</li> <li>○ International Auditor Regulatory Institute (established in 2007).</li> <li>○ Leadership roles in international organizations and regular participation in Enforcement and Inspection workshops of IAIAR.</li> <li>○ Coordination of cross-border information sharing, investigations and resources sharing.</li> </ul> </li> </ul>	<p>Board action taken to establish arrangements, participate in organizations and establish International Auditor Regulatory Institute, which holds annual meetings.</p>



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## Forum

### Are we there yet? Protecting investors by securing a strong auditing profession into the future



#### ARTICLE INFO

##### Keywords:

Audit regulation  
PCAOB  
Auditing profession  
Sarbanes–Oxley Act  
Audit quality  
Audit market concentration

#### ABSTRACT

In 2008, the U.S. Department of the Treasury's Advisory Committee on the Auditing Profession (ACAP) issued a report with findings and recommendations to address the sustainability and effectiveness of the public company auditing profession. The ACAP report addressed a number of longstanding issues and emerging developments at a critical time in history for the auditing profession and the Public Company Accounting Oversight Board (PCAOB). As the first comprehensive study of the profession since the Sarbanes–Oxley Act of 2002, the report identifies many significant issues for the PCAOB and the profession itself. The report dealt with three primary areas: human capital issues impacting the auditing profession, audit firm structure and finances, and audit firm concentration and competition. The report contains numerous recommendations directed toward regulators, academics, the auditing profession, and other stakeholders. This paper provides updated information about the numerous actions taken on sixteen ACAP recommendations that refer to or involve the PCAOB. Given the amount of effort related to these recommendations, it seems reasonable to ask, "Are we there yet?" But this is not the correct question, because we should never become complacent in thinking that we have made sufficient progress or completed the necessary actions to achieve and maintain high quality auditing. Since the time ACAP report was written, risks to audit quality have changed. The PCAOB continues to focus on areas raised in the ACAP report. While key issues raised in the ACAP report remain relevant, audit firms and audit regulators must be insightful and forward-looking to detect new and emerging risks so that timely actions can be taken to ensure reliable, high quality auditing to support the capital markets and protect investors. Numerous opportunities for future research exist in evaluating the impact of actions taken on the ACAP recommendations, including to what extent the actions have accomplished the original objectives and whether unanticipated consequences have occurred or additional actions might be needed.

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As a Board member of the U.S. Public Company Accounting Oversight Board (PCAOB), I spend considerable time and effort analyzing the sustainability and effectiveness of the audit in protecting investors and promoting confidence in the capital markets. I am also acutely aware of the remaining work that needs to be done to attain a resilient and strong profession that achieves those objectives, now and into the future.

The U.S. Department of the Treasury took a snapshot of these issues in a 2008 report by its Advisory Committee on the Auditing Profession (ACAP).

My objective in this paper is to provide a description of the PCAOB's actions related to the ACAP recommendations that refer to or involve the PCAOB, along with

contextual information to describe the background and basis for the recommendations. Because it had been years since such an analysis had been conducted,<sup>1</sup> my initial concern in starting this project was that I would find large issue areas within the ACAP recommendations that had yet to be addressed by the PCAOB. In fact, that is not the case. The amount of work conducted by the PCAOB related to the ACAP recommendations is impressive.

In some instances, the PCAOB actions taken differ from what was specifically indicated in a recommendation. It is important to keep in mind that the Committee's recommendations were made at a particular point in time and PCAOB actions have been taken after additional study and

<sup>1</sup> In 2010, the PCAOB staff prepared a paper on the status of the PCAOB-related ACAP recommendations of the October 13–14, 2010 Advisory Committee Meeting ([Public Company Accounting Oversight Board, 2010c](http://www.pcaobus.org/~/media/Files/2010/10/13-14_2010_ACM_Mtg_Paper.pdf)).

Presentation at the Braden Award Ceremony, October 9, 2015.

analysis of information that became available based on its regulatory oversight activities.

I am not presenting conclusions about the adequacy of the PCAOB actions in meeting the original intent and objectives of the ACAP recommendations, as such conclusions are better as the subject of research studies or policy debates. In addition, these topics and their impact need to be monitored over time within the context of the dynamic and changing environment of public company auditing. This is not simply a “check the box” exercise after which we can declare actions completed.

Therefore, what I endeavor to do in this paper is to provide information that will be useful to researchers in formulating specific research questions, as well as designing broad analyses related to the state of auditing and the profession now and in the future.

## Background

The accounting profession has been studied extensively over recent decades, frequently in response to scandals or other major problems. In 1996, the U.S. General Accounting Office (GAO)<sup>2</sup> issued a two-volume report (*General Accounting Office, 1996a, 1996b*) that summarized the results of 27 significant studies about the profession that were conducted from 1972 to 1995. The studies highlighted actions and reforms needed in the areas of auditor independence, the auditor’s responsibility for detecting fraud, the effectiveness of internal control, and ongoing challenges with accounting and auditing standard setting.

In the years immediately following the issuance of the GAO report, the U.S. capital markets experienced a wave of corporate financial reporting and auditing scandals. A full-blown crisis of restatements and heavy losses in market capitalization began in the late 1990s (*General Accounting Office, 2002*), followed by a string of corporate failures and financial accounting and auditing scandals. Two infamous companies served as the “bookends” for this string of scandals: Enron and WorldCom (*Franzel, 2014*). With the demise of their auditor, Arthur Andersen, concentration among the largest audit firms increased, as the number of dominant firms fell from the “Big 5” to the “Big 4.”

In response to the many scandals, on July 25, 2002, Congress passed the Sarbanes–Oxley Act of 2002, which President George W. Bush signed into law five days later.<sup>3</sup> The Act dealt with many of the issues identified over the decades as problematic in financial reporting and auditing for public companies.

Among other things, the Act created the PCAOB to oversee the audits of public companies to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports. Thus, audits of U.S. public companies and their auditors became subject to regulatory oversight for the first time in history. Previously this segment of the profession was self-regulated.

In 2010, to further promote investor protection, the Dodd–Frank Wall Street Reform and Consumer Protection Act amended the Sarbanes–Oxley Act to, among other things, give PCAOB the explicit authority to oversee the audits of brokers and dealers.

The PCAOB commenced operations in April 2003, and began the process of developing and implementing its statutory responsibilities, which now include:

- registering public accounting firms that audit public companies, brokers, or dealers;
- establishing auditing and other professional standards;
- conducting and reporting on regular inspections of registered public accounting firms that audit public companies, brokers, or dealers; and
- conducting investigations and disciplinary proceedings in cases where auditors may have violated certain provisions of the Act, the rules of the PCAOB and the Securities and Exchange Commission (SEC), and other laws, rules, and professional standards governing the audits of public companies, brokers, and dealers (*Public Company Accounting Oversight Board, 2015a, p. 1*).

## Treasury’s advisory committee on the auditing profession

In November 2006, Secretary of the Treasury Henry Paulson Jr. spoke about indicators of both persistent and newly emerging risks in the capital markets, including “questions about the [public company audit] industry’s sustainability and effectiveness” (*Paulson, 2006, p. C:8*). Secretary Paulson articulated growing concerns about the decline in corporate participation in the U.S. stock markets. He highlighted areas of study that provide a “framework to assess our own capital markets” (*Paulson, 2006, p. C:3*), which included concerns related to public company accounting and auditing.

Secretary Paulson suggested that there was evidence that recent regulatory reforms “may not be healthy” and may be “fundamentally altering the interactions between auditors and corporate management and boards in a number of ways, some of which are not constructive.” (*Paulson, 2006, p. C:8*). He also cited increasing market concentration among audit firms and a high number of corporate financial restatements.

Following additional outreach, Secretary Paulson announced in the spring of 2007 that the Department of the Treasury had developed and was beginning to implement a “capital markets action plan.” The first stage of the plan would involve the chartering of “a non-partisan committee to develop recommendations to consider options available to strengthen the [auditing] industry’s financial soundness and its ability to attract and retain qualified personnel” (*Department of the Treasury, 2007a*).

Thus, the Treasury Department established the Advisory Committee on the Auditing Profession (“the Committee”) in 2007. The Committee was charged with evaluating the sustainability of a strong and vibrant auditing profession and providing informed advice and recommendations to Treasury. The Committee was organized to study three broad areas:

<sup>2</sup> Now called the Government Accounting Office, the GAO is an independent, nonpartisan agency that works for the U.S. Congress and performs audits and investigations of federal agencies and programs.

<sup>3</sup> Public Law No. 107-204, July 30, 2002.

- (1) the auditing profession's ability to cultivate, attract, and retain the human capital necessary to meet developments in the business and financial reporting environment and ensure audit quality for investors;
- (2) the organizational structure, financial resources, and communication of the auditing profession; and
- (3) audit market competition and concentration and the impact of independence and other professional standards on this market and investor confidence (Department of the Treasury, 2007b).

The ACAP study represented the first comprehensive study of the auditing profession since the enactment of the Sarbanes–Oxley Act of 2002. While the Committee worked, however, a new financial crisis was brewing. The housing market and the related subprime mortgage market were experiencing turbulence, which evolved quickly through 2007 and 2008 into a significant liquidity crisis and a recession.

On October 6, 2008, the Committee issued its final report to the Treasury Department and Secretary Paulson with findings and recommendations to address concerns raised about the sustainability and effectiveness of the accounting and auditing profession (Department of the Treasury, 2008, p. II:1).

The ACAP report is organized around the three primary areas of Committee focus: human capital, audit firm structure and finances, and audit firm concentration and competition. The report contains 31 recommendations across these areas of focus. Within the recommendations are more detailed sub-recommendations, including 16 that refer to or involve the PCAOB.

The ACAP report is 219 pages long. Each recommendation is accompanied by extensive background information, context, and references. In this paper, I have added brief context for each of the major sections of the report and have paraphrased the recommendations. Although I have endeavored to be accurate and balanced in characterizing the Committee's recommendations and the related context, it will be useful for researchers and others who are interested in pursuing these topics to go back and review the original text of the ACAP report.

To my knowledge, notwithstanding the tireless efforts of many to advance the goals for improving the accounting and auditing profession since the issuance of the ACAP report, there has been no comprehensive monitoring and reporting on the overall progress related to the full breadth of the Committee's recommendations.

Recent efforts by the academic community to integrate accounting and auditing research, education, and practice have involved research on the relationship between the Committee's recommendations and existing audit research literature.<sup>4</sup>

Numerous opportunities for future research exist in evaluating the impact of actions taken on the ACAP recommendations, including to what extent the actions have

accomplished the original objectives and whether unanticipated consequences have occurred or additional actions might be needed. Study of actions taken in other jurisdictions may also be useful to help inform U.S. policy decisions on potential actions.

### ACAP recommendations related to PCAOB oversight

The PCAOB has taken numerous actions related to each of the 16 Committee recommendations that involve PCAOB oversight. Those actions take into account the evolving conditions in the capital markets and related developments in the accounting and auditing professions in the seven years since the issuance of the ACAP report.

Below is a description of these 16 recommendations – organized by the broad area of focus and including some background and context.

#### Human capital recommendations

The Committee noted that to ensure the viability and resilience of the public company audit profession and its ability to meet the needs of investors, the profession needs to continue to attract and develop professionals at all levels who are prepared to perform high quality audits in a dynamic environment. The Committee also recognized that several of its recommendations would have an impact beyond the public company auditing profession, impacting the accounting profession as a whole (Department of the Treasury, 2008, p. VI:1).

The Committee made five broad recommendations for action by regulators, educators, educational institutions, the auditing profession, and others in the area of human capital, which contained a number of sub-recommendations (Department of the Treasury, 2008, chap. VI). Table 1 summarizes these recommendations.

#### PCAOB recommendation #1

Make accounting faculty fellowship programs available at the PCAOB (Department of the Treasury, 2008, p. VI:22).

**Table 1**  
Committee recommendations related to auditing profession human capital.

1. Implement dynamic accounting curricula and certification exams to reflect market-driven, real-world developments and to help prepare new entrants to the profession to perform high quality audits.
2. Improve the recruitment and retention of minorities in the auditing profession and academia to enrich the pool of human capital in the profession. Emphasize the role of community colleges in recruitment of minorities to the profession and the use of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.
3. Ensure a sufficiently robust supply of qualified accounting faculty by increasing the supply, including professionally qualified faculty; emphasizing cross-sabbaticals; and improving incentives.
4. Develop and maintain consistent demographic and higher education program profile data.
5. Encourage the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association (AAA) to form a commission to study the future structure of higher education in the accounting profession.

<sup>4</sup> For example, a recent study highlighted the gap between research and practice by comparing each of the Committee's recommendations to the audit research literature and concluded that about half of the documented audit research themes were not covered by any Committee recommendation and seven of the Committee's recommendations were not directly addressed in the research literature (Ratzinger-Sakel & Gray, 2015).

*Background* The Committee heard concerns about the relevance of the knowledge and practical experience of accounting faculty. The ACAP report described the benefits of cross-sabbaticals, the exchange of experienced professionals and academics who provide “interactive relationships.” According to the Committee, “Evidence suggests that such exchanges can be beneficial, and continued development of such exchanges is expected to provide substantial benefits for all parties.” The Committee recommended expanding faculty fellowship programs in agencies, such as those at the SEC and the Financial Accounting Standards Board (“FASB”), and making them available at the PCAOB (Department of the Treasury, 2008, p. VI:16, 22).

*PCAOB actions* On December 22, 2009, the PCAOB announced the establishment of and candidate solicitation for an Academic Fellowship Program. This program is designed to appoint experienced researchers and academics with an active interest in auditing and oversight matters to serve as Academic Fellows for a term of up to 12 months.

Since 2009, the PCAOB has had three academic fellows under this program. They have provided analytical support, advice, and academic background information to the PCAOB Office of Research and Analysis (“ORA”) as well as other offices and divisions of the PCAOB. Each of the three fellows joined the PCAOB from, and subsequently returned to, academic teaching positions in accounting.

In 2013, the PCAOB announced the establishment of the Center for Economic Analysis to study and advise the Board and PCAOB staff on the role of the audit in capital formation and investor protection and how economic theory and analysis can be used and further developed to enhance the effectiveness of PCAOB programs (Public Company Accounting Oversight Board, 2013c). To support this objective, the PCAOB established within the Center an Economic Research Fellowship program to conduct economic research on auditing matters that will inform the oversight activities of the PCAOB in protecting investors (Public Company Accounting Oversight Board, 2014a).

The PCAOB has had four Economic Research Fellows to date. These fellows serve terms of 12 months, with the possibility of extending to 24 months. To be eligible, candidates should be current doctoral students or recent graduates with backgrounds in economics, finance, accounting, or related areas. Candidates submit research proposals to the PCAOB in areas related to the role and relevance of audits in the capital markets. Two of the PCAOB’s present Economic Research Fellows are incumbent accounting professors, and the other two are doctoral students.

Economic Research Fellows have an opportunity to publish their research under their own name (disclaimed by the PCAOB). Some of the research conducted by PCAOB fellows has generated working papers that may be submitted for publication.<sup>5</sup> Fellows also have access to PCAOB staff and Board members, and the opportunity to gain an inside understanding of the regulatory process. They see firsthand

the PCAOB’s emphasis on audit quality and investor protection, and participate in the PCAOB’s goal of fostering high quality research.

PCAOB fellows and other staff researchers and analysts also have regular opportunities to engage with the academic community and researchers at other regulatory organizations (Franzel, 2016).

#### *Firm structure and finances recommendations*

The Committee’s second area of focus was the sustainability of the auditing profession, which included a number of matters directly related to audit firm structure, such as governance, transparency, global organization, financial strength, and ability to access capital. This area of focus also included audit quality, the investing public’s understanding of auditors’ responsibilities and communications; the limitations of audits, particularly relating to fraud detection and prevention; the effect of litigation where audits are alleged to have been ineffective; and the regulatory system applicable to auditing firms (Department of the Treasury, 2008, 2008, p. VII:1).

The Committee made seven broad recommendations in this area to regulators, the auditing profession, and others, which contained a number of sub-recommendations (Department of the Treasury, 2008, chap. VII). Table 2 summarizes these recommendations.

**Table 2**  
Committee recommendations related to firm structure and finances.

1. Urge the SEC and Congress, as appropriate, to provide for the creation by the PCAOB of a national center to focus on fraud prevention and detection.
2. Encourage greater regulatory cooperation among the SEC, the PCAOB, state boards of accountancy, and other government regulators to improve regulatory effectiveness and reduce duplication and inconsistency. At the state level, improve mobility of CPA licenses across states, and improve the independence of the state boards of accountancy.
3. Urge the PCAOB and SEC, in consultation with relevant stakeholders, to explore the possibility of firms appointing independent members with full voting power to firm Boards and/or advisory Boards with meaningful governance responsibilities to improve the governance and transparency of auditing firms.
4. Urge the SEC to amend Form 8-K disclosure requirements to characterize and report appropriately every public company auditor change and require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audits.
5. Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor’s reporting model, including clarification of the auditor’s role in detecting fraud and potentially expanding the audit report.
6. Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner’s signature on the auditor’s report.
7. Urge the PCAOB to require large auditing firms to produce a public annual report incorporating information about firm structure, client lists, independence practices, financial information, and the effectiveness of the firm’s control systems, similar to what is required by the European Union’s Eighth Directive. Such reporting would also include key indicators of audit quality, as determined by the PCAOB. Further urge that PCAOB require the larger auditing firms to file with the PCAOB on a confidential basis audited financial statements.

<sup>5</sup> The PCAOB makes these papers available on its website at <http://pcaobus.org/About/CenterforEconomicAnalysis/Pages/Working-Papers.aspx>.



### PCAOB recommendation #2

Urge the SEC and the Congress, as appropriate, to provide for the creation by the PCAOB of a national center to (1) facilitate auditing firms and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies; and (2) commission research and other fact finding regarding fraud prevention and detection, and further the development of best practices regarding fraud prevention and detection (Department of the Treasury, 2008, p. VII:1).

*Background* The Committee noted that no formal forum currently exists where auditors and other market participants regularly share their views and experiences relating to fraud prevention and the detection of fraudulent financial reporting. The Committee stated that it “believes that a collective sharing of fraud prevention and detection experiences among auditors and other market participants will provide a broad view of auditor practices and ultimately improve fraud prevention and detection capabilities and enable the development of best practices. The Committee also believes that research into industry trends and statistics will help auditors focus and develop procedures to identify areas and situations at greater risk for fraud” (Department of the Treasury, 2008, p. VII:2).

*PCAOB actions* The PCAOB developed a preliminary outline for a center, and included funding in its 2009 budget for a “National Fraud Center” (Public Company Accounting Oversight Board, 2008b, p. 1). On April 6, 2010, the PCAOB posted an announcement soliciting candidates for a position of director of the new center.

At the inaugural meeting of the Board's Investor Advisor Group (“IAG”) on May 4, 2010, the Board sought input on the establishment of a fraud center. At that meeting, the Board heard a range of suggestions for the possible mission, functions, and operations of the center, many of which reflected considerations related to the recent financial crisis (Public Company Accounting Oversight Board, 2010a, pp. 1–3).

The PCAOB, however, did not move forward with plans to establish a center. Following a strategy announced later that year in its 2010–2014 strategic plan (Public Company Accounting Oversight Board, 2010d, p. 24), the PCAOB decided to continue to study the Committee's recommendation.

Beginning in 2012, the Board's standard-setting staff renewed efforts in this area through consideration of approaches to conducting outreach and potential standard-setting projects related to the role and responsibilities of auditors in the area of fraud (Public Company Accounting Oversight Board, 2012a, pp. 2–3; Public Company Accounting Oversight Board, 2012c).

In 2013, the Board discussed with its SAG the potential of establishing a SAG task force related to conducting outreach or research on the auditor's responsibility for detecting financial statement fraud (Public Company Accounting Oversight Board, 2013d). Among the approaches discussed, the Board considered conducting research through its new Center for Economic Analysis and its Office of Research and Analysis into the economic consequences of fraud.

The November 2014 SAG meeting included panel discussions on research and other experiences related to the

detection and impact of fraud, and a discussion of the preliminary results of PCAOB staff research related to the auditor's approach to detecting material misstatements due to fraud (Public Company Accounting Oversight Board, 2014d).

PCAOB staff, coordinated through the PCAOB Center for Economic Analysis, is currently developing a strategy to analyze evidence, research, and data related to financial statement fraud. In particular, the PCAOB's current strategic plan articulates a strategy to use the Center to enhance the use of economic analysis, empirical tools, and analysis to “analyze evidence, research, and data related to the auditor's approach to detecting financial statement fraud, economic impacts of financial statement fraud, and trends in financial statement fraud and seek to encourage further academic research in these areas” (Public Company Accounting Oversight Board, 2015d, pp. 20–21).

This new strategy provides opportunities for the PCAOB and interested researchers and stakeholders to develop a clearer understanding of the current state of knowledge related to the causes and impact of financial statement fraud, and to identify relevant research and policy questions associated with detecting and preventing such fraud, including the role of the auditor (Franzel, 2016).

### PCAOB recommendation #3

Require regular and formal roundtables of the PCAOB, the SEC, the Department of Justice (DOJ), the state boards of accountancy, and the state attorneys general to periodically review the overall enforcement regimes applicable to the public company auditing profession and focus on regulatory coordination to reduce the incidence of duplication and potentially inconsistent enforcement regimes (Department of the Treasury, 2008, p. VII:7).

*Background* “The Committee believes that enhancing regulatory cooperation and reducing duplicative oversight of the auditing profession by federal and state authorities and enhancing licensee practice mobility among the states are in the best interest of the public and the effective operation of the capital markets” (Department of the Treasury, 2008, p. VII:4).

*PCAOB actions* Although no specific requirement has been put in place, the Board and the PCAOB staff coordinate and meet regularly with various regulators to discuss respective oversight responsibilities.

For example, PCAOB staff shares information about PCAOB inspection and enforcement matters, as appropriate, with state boards of accountancy, and the Board meets periodically with representatives of the National Association of State Boards of Accountancy (NASBA). The PCAOB Division of Enforcement and Investigations meets on a regular basis with staff of the SEC Enforcement Division to coordinate investigative activities. In addition, PCAOB staff coordinates with DOJ, state and federal financial regulators, and law enforcement authorities on individual enforcement cases, as appropriate.

### PCAOB recommendation #4

Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze,

explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve the governance and transparency of auditing firms (Department of the Treasury, 2008, p. VII:8).

*Background* The Committee stated its belief that enhancing corporate governance of auditing firms through the appointment of independent members to their advisory boards and/or to firm boards, “whose duties run to the auditing firm and its partners,” could be particularly beneficial to audit firm management and governance. “The Committee also believes that such advisory boards and independent board members could improve investor protection through enhanced audit quality and firm transparency.”

The Committee acknowledged that there are “multiple challenges” and many factors for the PCAOB, SEC, and other state and federal regulators to consider in responding to its recommendation (Department of the Treasury, 2008, p. VII:10).

*PCAOB actions* At a May 4, 2010 PCAOB IAG meeting, the Board sought input from the IAG on the topic of greater transparency and governance of audit firms (Public Company Accounting Oversight Board, 2010a, pp. 4–6). Among the issues raised as part of this discussion was the use of firm advisory boards composed of individuals who are independent from the audit firm.

The Board subsequently discussed this and other audit firm governance and transparency matters with the IAG in 2011 and 2013. In the latter discussion, the IAG presented information to the Board about the recent implementation by global audit firms of requirements in the U.K. for the appointment of independent non-executive directors to the boards of the firms regulated by the U.K. Financial Reporting Council (Public Company Accounting Oversight Board, 2013b, pp. 20–24).

While the Board has not taken further formal actions on this recommendation, some of the member audit firms of the largest global networks have implemented aspects of these recommendations beyond those required by the U.K. For example, in the U.S., Deloitte LLP reported that it has established an advisory council comprised of outside members. Two of the largest global network umbrella organizations, Ernst & Young Global Limited and Grant Thornton International Limited, have reported including external members on their advisory councils.

#### *PCAOB recommendation # 5*

Require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audits and, other than for retirement, the reasons for those changes (Department of the Treasury, 2008, p. VII:11).

*Background* The Committee received testimony and commentary that viewed the lack of transparency surrounding auditor changes as detrimental to investor confidence in financial reporting.

*PCAOB actions* The Board’s inspection staff obtains engagement partner information (and other audit firm staff information)

from audit firms that it inspects. Information about engagement partners, among other factors, is used in making risk-based selections of audit engagements for inspections (Public Company Accounting Oversight Board, 2013e, p. 7).

In a final rule adopting that proposal on December 15, 2015, the Board established rules to require the public disclosure of the name of the engagement partner on each completed audit (Public Company Accounting Oversight Board, 2015f).<sup>6</sup> The Board noted that, “The disclosures being adopted by the Board will reveal engagement partner rotations to investors, including instances where engagement partners left the engagement before rotation would have been required” (Public Company Accounting Oversight Board, 2015f, p. 54).

#### *PCAOB recommendation #6*

Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor’s standard reporting model. Further, urge that the PCAOB clarify in the auditor’s report the auditor’s role in detecting fraud under current auditing standards (Department of the Treasury, 2008, p. VII:13).

*Background* The Committee described the standardized audit report that has reflected a “pass/fail model” since the 1930s. In that context, the Committee heard testimony concerning the longstanding “expectations gap” between investors and auditors, which the Committee understood to be “defined as ‘the difference between what the public and users of financial statements perceive the role of an audit to be and what the audit profession claim[s] is expected of them during the conduct of an audit’” (Department of the Treasury, 2008, p. VII:14).

The Committee described potential concerns related to the lack of clarity regarding the role and responsibilities of the auditor, as well as the extent of work and limitations of the audit.

The Committee also noted that over the years there have been numerous recommendations that the standard auditor’s report be improved, including a clarification of the auditor’s responsibilities as well as an expansion of the auditor’s report to include information about how the auditor reached its opinion.

*PCAOB actions* On August 13, 2013, the Board proposed a new standard and amendments to existing standards to enhance the auditor’s report to provide more useful information to investors and other financial statement users. The Board’s proposal would retain the pass/fail model, including the basic elements of the current auditor’s report, and would provide more information to investors and other financial statement users about the audit and the auditor.

Most significantly, the proposed auditor reporting model standard would require the auditor to communicate in the auditor’s report “critical audit matters” specific to each audit. The auditor’s required communication would focus on those matters the auditor addressed during the audit of the financial statements that involved the most difficult, subjective, or

<sup>6</sup> The Board’s rules are subject to the approval of the SEC. As of the date of this publication, the SEC had not yet acted on the Board’s final rule.



complex auditor judgments or posed the most difficulty to the auditor in obtaining sufficient appropriate audit evidence or forming an opinion on the financial statements ([Public Company Accounting Oversight Board, 2013a](#), pp. 5–6).

The proposal would also require auditors' reports to clarify the descriptions of the auditor's responsibilities to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud.

The proposal followed years of outreach to investors, public companies, auditors, and others, as described in the proposing release. Following the issuance of the proposal, the Board met with its SAG and held a public roundtable to discuss the proposal and related developments in other countries.<sup>7</sup>

The PCAOB staff has analyzed the comments received on the proposal and at the public meetings and is drafting a reproposal for the Board's consideration. The staff anticipates recommending that the Board issue a reproposal of the auditor's reporting model standard for public comment in the second quarter of 2016.

#### PCAOB recommendation #7

Recommend that the PCAOB review the auditing standards governing fraud detection and fraud reporting and that the PCAOB periodically review and update these standards (Department of the Treasury, 2008, p. VII:13).

*Background* The Committee described potential concerns related to the auditor's responsibility and capability to detect fraud in an audit. The Committee acknowledged concerns about auditor performance in detecting fraud: "Public investors have appropriately raised questions when large frauds have gone undetected" ([Department of the Treasury, 2008](#), p. VII:14).

*PCAOB actions* The Board has taken a number of steps and has actions ongoing in this area.

Beginning in 2010, the Board issued several auditing standards that relate to auditors' responsibilities to assess and respond to certain fraud risks.

*Risk assessment standards integrating auditor's responsibility for fraud* On August 5, 2010, the Board adopted eight auditing standards related to the auditor's assessment of and response to risk in an audit ([Public Company Accounting Oversight Board, 2010b](#)). Among other things, the standards integrate the auditor's responsibilities for considering fraud during the audit. This integration emphasizes that consideration of fraud is a central part of the audit process and should prompt auditors to make a more thoughtful and thorough assessment of fraud risks and develop appropriate audit responses. The standards also include additional requirements related to consideration of potential management bias in financial statements and fraud risks regarding omitted, incomplete, or inaccurate disclosures. The standards became

effective for audits of fiscal periods beginning on or after December 15, 2010.

*Related parties and significant unusual transactions* On June 10, 2014, the Board adopted a new auditing standard (Auditing Standard No. 18) and amended other auditing standards to strengthen auditor performance requirements in three critical areas that historically have represented increased risks of material misstatement in company financial statements: related parties, significant unusual transactions, and a company's financial relationships and transactions with its executive officers ([Public Company Accounting Oversight Board, 2014b](#)). These have been contributing factors in numerous financial reporting frauds over the last several decades. The standards became effective for audits of financial statements for fiscal years beginning on or after December 15, 2014.

*Audit practice alerts and summary inspection reports* The PCAOB issues Staff Audit Practice Alerts to highlight new, emerging, or other timely matters – including fraud risks – that may affect how auditors conduct audits under the existing requirements of PCAOB standards and relevant laws. Recent Practice Alerts highlighted frequent PCAOB inspection findings in areas that are associated with fraud risks.

- Staff Audit Practice Alert No. 12, *Matters Related to Auditing Revenue in an Audit of Financial Statements* ([Public Company Accounting Oversight Board, 2014c](#)), described recently identified audit deficiencies in the area of the auditors' responses to risk of material misstatement due to fraud associated with revenue.
- Staff Audit Practice Alert No. 10, *Maintaining and Applying Professional Skepticism in Audits* ([Public Company Accounting Oversight Board, 2012d](#)), described recent audit deficiencies in which auditors failed to exercise professional skepticism in response to identified fraud risks.

In addition, the Board issues general reports in which it summarizes audit deficiencies identified by PCAOB inspections staff, including common deficiencies in areas involving fraud risks.

*Outreach and research* In addition, as described earlier in connection with the Committee recommendation to establish a national fraud center, the PCAOB standard-setting staff and researchers continue to engage in outreach and research related to the auditor's responsibilities and effectiveness at detecting financial statement fraud.

#### PCAOB recommendation #8

Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report ([Department of the Treasury, 2008](#), p. VII:19).

*Background* The Committee noted that the PCAOB had previously discussed with its SAG – as part of a broader discussion of potential changes to the auditor's reporting model – whether audit engagement partners and concurring partners should sign the auditor's report in their own names. The Committee also

<sup>7</sup> The transcripts of these meetings are available on the PCAOB website under Rulemaking Docket #34: <http://pcaobus.org/Rules/Rulemaking/Pages/Docket034.aspx>.

noted that engagement partner signatures were required in other jurisdictions, primarily in Europe.

The Committee reported its belief “that the engagement partner’s signature on the auditor’s report would increase transparency and accountability.” However, citing safe harbor provisions promulgated by the SEC in its rulemaking related to public company audit committee financial experts, the Committee noted that “the signature requirement should not impose on any signing partner any duties, obligations or liability that are greater than the duties, obligations and liability imposed on such person as a member of an auditing firm” (Department of the Treasury, 2008, p. VII:20).

*PCAOB actions* On December 15, 2015, the Board adopted new rules to provide investors with more information about the participants in public company audits, including disclosure of the name of the engagement partner for each issuer audit, as well as the names of other audit firms that participated in each audit, on a new PCAOB form “AP” (Public Company Accounting Oversight Board, 2015f).

The Board began this rulemaking process in 2009, in response to the ACAP recommendation, by seeking comment on whether the engagement partner should be required to sign the auditor’s report (Public Company Accounting Oversight Board, 2009).

Throughout the process, the Board sought to balance the potential benefits of disclosure regarding the engagement partner name and the names of other accounting firms that participate in the audit with concerns expressed by some commenters about potential consequences, including the potential for an increase in auditor liability and litigation risk, confusion about the role of the firm in the audit, and administrative costs, among other concerns.

In 2011, after considering commenters’ views on a signature requirement, the Board proposed rules to require disclosure in the auditor’s report of the name of the engagement partner. The Board proposed a disclosure approach instead of a signature requirement primarily in response to commenters’ concerns regarding liability and the potential for a signature to overemphasize the role of the engagement partner in relation to that of the firm as a whole. In addition, the Board proposed rules to require disclosures about accounting firms and other participants in the audit to provide investors and other financial statement users with greater transparency regarding other firm participants in the audit (Public Company Accounting Oversight Board, 2011).

In December 2013, the Board repropoed amendments to its standards to require disclosure in the auditor’s report of: (1) the name of the engagement partner; (2) the names, locations, and extent of participation of other independent public accounting firms that took part in the audit; and (3) the locations and extent of participation, on an aggregate basis by country, of certain nonaccounting firm participants in the audit (Public Company Accounting Oversight Board, 2013e).

In June 2015, the Board sought comment on the possibility of mandating these disclosures on a new PCAOB form, Form AP, as an alternative to mandated disclosure in the auditor’s report. The 2015 Supplemental Request also solicited comment on narrowing or eliminating disclosures

regarding nonaccounting firm participants (Public Company Accounting Oversight Board, 2015b).

The Board adopted new rules based on the 2015 Supplemental Request, with certain technical adjustments and phased effective dates for the disclosures related to engagement partners and other accounting firms participating in the audit. As the Board’s adopting release explains: “The requirement to provide disclosure on Form AP, rather than in the auditor’s report as previously proposed, is primarily a response to concerns raised by some commenters about potential liability and practical concerns about the potential need to obtain consents for identified parties in connection with registered securities offerings.... The Board believes that providing information about the engagement partner and the other accounting firms that participated in the audit on Form AP, coupled with allowing voluntary reporting in the auditor’s report, will achieve the objectives of enhanced transparency and accountability for the audit while appropriately addressing concerns raised by commenters” (Public Company Accounting Oversight Board, 2015f, p. 6).

#### *PCAOB recommendation #9*

Urge the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating information required by the European Union’s Eighth Directive, Article 40 Transparency Report and key indicators of audit quality and effectiveness, as determined by the PCAOB. Further, urge the PCAOB to require that, beginning in 2011, larger auditing firms file with the PCAOB, on a confidential basis, audited financial statements. Also recommend that the PCAOB determine which of the requirements covered by the recommendation should be extended to smaller audit firms (Department of the Treasury, 2008, p. VII:20, 23).

*Background* The Committee noted that auditing firms and investors have expressed support for requiring U.S. auditing firms to publish reports similar to the Article 40 Transparency Report from the EU’s Eighth Directive. Under Article 40, public company auditors are required to post on their websites annual reports that include the following information: legal and network structure and ownership description; governance description; most recent quality assurance review; public company audit client list; independence practices and confirmation of independence compliance review; continuing education policy; financial information, including audit fees, tax advisory fees, consulting fees; and partner remuneration policies. The Article 40 Transparency Report also requires a description of the auditing firm’s quality control system and a statement by firm management on its effectiveness.

*Status* During the conduct of the Committee’s work, the PCAOB finalized rules, proposed in May 2006, that establish a reporting framework for registered firms, under which firms are required to file annual and special periodic reports with the PCAOB, portions of which would be publicly available (Public Company Accounting Oversight Board, 2008a). Although these reporting requirements were not in response to the ACAP recommendations, the Committee noted that some of the PCAOB requirements include elements similar to some of the requirements of the EU directive, such

as annual reports on firms' public company audit client lists and information about fees from public company clients for audit, tax, and non-audit services (Department of the Treasury, 2008, p. VII:21).

The PCAOB has heard on several occasions from its IAG various views on the merits and considerations related to requiring audit firms to provide more transparency into their finances, governance, and audit practices.

Although the Board has made substantial progress in considering potential audit quality indicators (AQIs) (as discussed below), the Board has not taken further actions in this area. Some firms, however, have begun disclosing and discussing various AQIs in their transparency reports. The Center for Audit Quality has provided guidance for firms to disclose certain audit quality information (Center for Audit Quality, 2013, p. 1).

Several foreign jurisdictions require audit firm transparency reports, including most European member states, consistent with EU directives and regulations, as well as Australia. The global network firms and their member affiliates in many of these jurisdictions issue separate transparency reports. In addition, most of the U.S. and Canadian member firms issue transparency reports, in part to comply with requirements of some EU member states in connection with audit services they provide in those jurisdictions.

#### *Concentration and competition recommendations*

The third area of focus of the Committee was public company audit market concentration and competition and the lack of choice of auditors in the large public company audit market, and the potential negative impact on audit quality and effectiveness (Department of the Treasury, 2008, p. VIII:1). The Committee heavily references two significant studies conducted by GAO regarding concentration and competition in the audit market (Government Accountability Office, 2003, 2008). The Committee also summarized testimony regarding perceived improvements in audit quality after enactment of the Sarbanes–Oxley Act as well as the risks associated with any adverse financial event affecting one of the large audit firms.

The Committee made six broad recommendations to regulators, the audit profession, and other bodies, which contained a number of sub-recommendations (Department of the Treasury, 2008, chap. VIII). Table 3 summarizes these recommendations.

#### *PCAOB recommendation #10*

When PCAOB inspectors interview the audit committee chair in connection with an inspection of an audit engagement at a company that has undergone a change of auditors, the PCAOB should inquire about whether the transition process was cooperative and transparent (Department of the Treasury, 2008, p. VIII:5).

*Background* The ACAP noted that some commentators cited the costs associated with public companies' changing auditors and how those costs can pose a barrier to entry for smaller firms trying to enter the larger public company audit market. The Committee noted that prompt and coordinated actions and communications among the company and

**Table 3**

Committee recommendations related to concentration and competition.

1. Reduce barriers to growth for smaller firms. Require disclosure by public companies of any provisions in agreements with third parties that limit auditor choice. Include representatives of smaller audit firms in regulatory meetings, outreach, and other engagement.
2. Monitor potential sources of catastrophic risk in large firms and establish a mechanism for rehabilitation of a troubled, larger audit firm.
3. A determination by the PCAOB, in consultation with stakeholders, of the feasibility of developing key indicators of audit quality and requiring firms to publicly disclose these indicators. Require the PCAOB to monitor such indicators.
4. Promote understanding of and compliance with auditor independence requirements by compiling requirements into a single document that is website accessible. Develop training materials to foster healthy professional skepticism with respect to the lack of independence and other conflicts among public company auditors. Use the PCAOB inspection process to inspect for these issues.
5. Adopt annual shareholder ratification of auditors for all public companies.
6. Enhance regulatory collaboration between PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the U.S.

predecessor and successor auditors can reduce perceived obstacles and costs related to auditor changes (Department of the Treasury, 2008, p. VIII:4–5).

*PCAOB actions* In 2010, the PCAOB staff noted that predecessor–successor auditor communications are discussed with firms and audit committee members as part of the inspection process (Public Company Accounting Oversight Board, 2010c, p. 11). The staff continues to make inquiries when there is a change in auditor about the cooperativeness and transparency of the transition process.

#### *PCAOB recommendation #11*

Recommend that regulators and policymakers, such as the PCAOB... include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements (Department of the Treasury, 2008, p. VIII:8–9).

*Background* The ACAP received testimony and comment letters suggesting that there should be greater inclusion and participation of smaller firms in public and private sector committees, roundtables, and fellowships. The Committee stated that “increasing name recognition and reputation could promote audit market competition and auditor choice” (Department of the Treasury, 2008, p. VIII:8).

*PCAOB actions* The PCAOB includes representatives of smaller audit firms on its advisory groups and in public meetings.

The Board also conducts outreach to smaller audit firms through its forums on auditing in the small business environment and forums on auditing brokers-dealers. These forums are designed to share important information about Board activities with PCAOB-registered public accounting firms that audit smaller public companies and SEC-registered broker-dealers. The forums also provide an opportunity for

Board members and PCAOB staff to hear comments, concerns, and questions from auditors.

Recently, the PCAOB began an outreach initiative using webinars to deal with important time-sensitive issues and to make it more efficient and cost-effective for auditors, investors, audit committee members, and others to receive PCAOB updates. The live, interactive webinars, which are recorded and available for viewing on the PCAOB website, also provide continuing professional education credit to members of registered firms.

#### *PCAOB recommendation #12*

As part of its current oversight of registered auditing firms, the PCAOB should monitor potential sources of catastrophic risk that would threaten audit quality ([Department of the Treasury, 2008](#), p. VIII:10).

*Background* The Committee concluded that “the loss of one of the larger auditing firms would likely have a significant negative impact on the capital markets.” The Committee further observed that the PCAOB’s audit quality-focused mission is intertwined with issues of catastrophic risk, as risks to firms’ survival historically have been largely the result of significant audit quality failures. In its explanatory comments, the Committee stated that the “objective of PCAOB monitoring would be to alert the PCAOB to situations in which auditing firm conduct is resulting in increased catastrophic risk which is impairing or threatens to impair audit quality” ([Department of the Treasury, 2008](#), p. VIII:10–11).

*PCAOB actions* In 2014, the Board added to its strategic plan an action item to monitor and analyze the business models of audit firms and any related risks to audit quality ([Public Company Accounting Oversight Board, 2014e](#), p. 13). In December 2015, the Board refined this strategy to consider specific risks posed by the evolving business models of the largest firms.

PCAOB research staff in ORA, working across the PCAOB, study a wide range of issues related to the business models of audit firms. Those issues include revenue and growth, scope and scale of practice, economics, competition, governance, incentives, staffing, processes, technology, and emerging trends. The goal is to identify features of the business model that promote audit quality, which the Board may encourage, and features that may threaten audit quality, which the Board may consider and address. The results of the research inform both shorter-term tactical decisions and longer-term priorities and strategy.

ORA also plans to report on the evolution and structure of larger accounting firms, including the mix of audit and non-audit services, and any implications of their multidisciplinary business models on independence and audit quality ([Public Company Accounting Oversight Board, 2015d](#), p. 13).

PCAOB inspections evaluate aspects of firms’ systems of quality control that could contribute to systemic noncompliance with professional standards. Deficiencies in firms’ systems of quality control are not publicly disclosed by the PCAOB unless a firm fails to address the deficiencies to the Board’s satisfaction within 12 months. The Board’s quality control inspection and remediation review processes are central to promoting audit quality and compliance with

professional standards ([Public Company Accounting Oversight Board, 2012b](#), pp. 8–9, A-9).

Finally, the Board and the PCAOB staff meet on a regular basis with leadership of the domestic member firms of the largest global networks to discuss these and other matters related to audit quality and practice.

#### *PCAOB recommendation #13*

Recommend that the PCAOB, in consultation with auditors, investors, public companies, audit committees, boards of directors, academics, and others, determine the feasibility of developing key indicators of audit quality and effectiveness and require auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators ([Department of the Treasury, 2008](#), p. VIII:14).

*Background* The Committee noted that a key issue in the public company audit market is consideration of what drives competition for audit clients; it acknowledged general uncertainty about whether audit quality is the most significant driver. The Committee stated its belief that requiring firms to disclose indicators of audit quality may enhance not only the quality of audits provided by such firms, but also the ability of smaller auditing firms to compete with larger auditing firms. The Committee also recognized the challenges of developing and monitoring audit quality indicators given the complexity of the audit process and environment ([Department of the Treasury, 2008](#), p. VIII:14–15).

*PCAOB actions* On July 1, 2015, after significant Board and staff outreach, the Board issued a concept release seeking public input on a conceptual framework for audit quality indicators that could potentially achieve objectives similar to those identified by the Committee ([Public Company Accounting Oversight Board, 2015c](#)).

The framework presents a portfolio of 28 potential measures related to three components of an audit: audit professionals, audit process, and audit results. It is premised on a broad definition of audit quality that takes into account varying perspectives that have been articulated over the decades by academics, other regulatory bodies, and the auditing profession.

The Concept Release sought input on some fundamental questions about this framework and the potential uses of audit quality indicators.

On November 12, 2015, ORA staff discussed this initiative with the Board’s SAG. ORA staff summarized the general themes raised in the 47 comment letters received on the concept release, including areas of general agreement and areas of controversy and differing views. The SAG discussed issues related to the content and possible uses of indicators, and then discussed possible next steps in the project. The PCAOB staff is analyzing the points raised and advice received.<sup>8</sup>

<sup>8</sup> Details about the topics of discussion and a summary of public comments received by the Board, together with a webcast and transcript of the SAG meeting, are available on the PCAOB website at [http://pcaobus.org/News/Events/Pages/Nov\\_2015\\_SAG.aspx](http://pcaobus.org/News/Events/Pages/Nov_2015_SAG.aspx).



*PCAOB recommendation #14*

Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible (Department of the Treasury, 2008, p. VIII:18).

*Background* The recommendation is part of the ACAP's broader recommendation to promote an understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit committees, and boards of directors, to enhance investor confidence in the quality of audit processes and audits (Department of the Treasury, 2008, p. VIII:17–18).

*PCAOB actions* PCAOB staff has discussed with SEC staff and the Board's SAG the considerations and challenges of the Committee recommendation to compile and publish the SEC and PCAOB's independence requirements in a single document. The PCAOB has expressed a commitment to future work on this effort in connection with future standard-setting projects.<sup>9</sup>

In addition, as discussed in more detail below, the Board's recent strategic plans have set forth a number of strategies to monitor compliance with independence requirements and enhance the independence of auditors. This includes continuing to hold auditors accountable for compliance with independence requirements and identifying the root causes of any noncompliance (Public Company Accounting Oversight Board, 2015d, pp. 17–18).

*PCAOB recommendation #15*

Through the PCAOB inspection process, inspect the firms' training related to professional skepticism with respect to issues of independence and other conflicts (Department of the Treasury, 2008, p. VIII:19).

*Background* The Committee heard testimony that "some auditors may be taking a 'check the box' approach to compliance with independence requirements, and losing focus on the critical need to exercise independent judgment or professional skepticism about whether the substance of a potential conflict of interest may compromise integrity or objectivity, or create an appearance of doing so" (Department of the Treasury, 2008, p. VIII:19) In that context, the Committee recommended that audit firms develop appropriate training materials to help foster and maintain the application of healthy professional skepticism with a focus on lessons learned through PCAOB oversight activities.

*PCAOB actions* Inherent within the PCAOB inspection process is an evaluation of a firm's application of professional skepticism. As part of that evaluation, inspection staff routinely evaluates firms' processes to improve the application of professional skepticism, including staff training, guidance, additional review, and other processes.

<sup>9</sup> The Board stated that it plans to undertake future standard-setting projects to address the organizational structure of its independence standards in its *Proposed Framework for Reorganization of PCAOB Auditing Standards*, PCAOB Release No. 2013-002, p. 16, March 26, 2013.

The PCAOB has included in its recent strategic plans a number of activities to enhance auditor independence, objectivity, and professional skepticism, including focused inspection oversight, monitoring approaches by audit firms and foreign regulators, and emphasizing the study of root causes of audit deficiencies identified in inspections (Public Company Accounting Oversight Board, 2015d, pp. 17–18).

In connection with those activities, the Board and staff have issued reports and Staff Audit Practice Alerts that emphasize the importance of independence, objectivity, and professional skepticism in audits and describe common audit deficiencies that involve failures in those areas. For example, Staff Audit Practice Alert No. 10, *Maintaining and Applying Professional Skepticism in Audits* (Public Company Accounting Oversight Board, 2012d), describes concerns among PCAOB staff about the potentially inconsistent and insufficient exercise of professional skepticism in critical audit areas.

In fact, Board members have "rolled up our sleeves" to talk about these issues publicly, in speeches and at other forums, and remind auditors and others about the objectives and fundamental requirements related to the exercise of professional skepticism (Franzel, 2013).

In addition, the PCAOB Division of Enforcement and Investigations considers as a "high priority" the investigation of potential auditor misconduct that involves issues of independence, objectivity, and professional skepticism (Public Company Accounting Oversight Board, 2015d, pp. 17, 42).

Of particular focus for Enforcement in recent years has been a high rate of noncompliance by auditors of brokers and dealers with applicable independence requirements. The Board has undertaken several initiatives to enhance compliance with these requirements and other professional standards, including issuing progress reports that describe significant observations from inspections, issuing guidance for audit and attestation engagements of brokers and dealers, conducting forums and webcasts, participating in various other outreach initiatives, and initiating investigations and disciplinary proceedings as appropriate.

*PCAOB recommendation #16*

Enhance regulatory collaboration and coordination between the PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the U.S. (Department of the Treasury, 2008, p. VIII:21).

*Background* The Committee described trends in the globalization of the capital markets and the involvement of multiple jurisdictions in the regulation of auditing. It also recognized the PCAOB's progress in coordinating with foreign audit regulators. The Committee stated its belief that "... these types of global regulatory coordination and cooperation are important elements in making sure public company auditing firms of all sizes are contributing effectively to audit quality." The Committee "urges the PCAOB and its foreign counterparts to continue to improve regulatory cooperation and coordination on a global basis" (Department of the Treasury, 2008, p. VIII:22).

*PCAOB actions* The PCAOB has continued to expand its collaboration and cooperation with foreign audit regulators as

it has expanded its international inspections and investigative activities. Currently, over 900 non-U.S. audit firms from more than 85 countries have registered with the PCAOB.

The PCAOB's recent strategic plans include activities intended to enhance relationships with regulators around the world. These include reaching agreements with additional foreign regulators on approaches to conducting joint inspections and strengthening existing relationships; participating as leaders in the International Forum of Independent Audit Regulators (IFIAR) to facilitate sharing of knowledge; and coordinating cross-border information sharing, investigations, regulatory policy, and analyses ([Public Company Accounting Oversight Board, 2015d](#), pp. 11, 13, 15–16).

On December 2, 2015, the PCAOB convened its ninth International Auditor Regulatory Institute, drawing more than 80 representatives from auditor oversight bodies and government agencies in 33 non-U.S. jurisdictions and five international organizations ([Public Company Accounting Oversight Board, 2015e](#)).

The Institute provides attendees the opportunity to enhance cross-border cooperation while sharing ideas and strategies for successful audit oversight. This year, more than a dozen representatives of other U.S. regulatory bodies and government agencies, and a number of representatives from academia and the private sector, engaged in a robust dialog through formal presentations on current audit issues.

The PCAOB also has taken on significant leadership roles with IFIAR, including Board members and staff serving as chair (Board member Lewis Ferguson), vice chair (Board member Ferguson and former Board member Daniel Goelzer), Advisory Committee members (PCAOB Chairman James Doty), chairs of working groups (Board members Ferguson and Steven Harris), and vice chairs of working groups (Director of Enforcement and Investigations Claudius Modesti).

## Conclusion

Given the extensive PCAOB actions related to the ACAP recommendations, it seems reasonable to ask, “Are we there yet?” But this is not the correct question, because we should never become complacent in thinking that we've made sufficient progress or completed the necessary actions to achieve high quality auditing. A nimble and responsive regulator should continually monitor relevant environmental and market conditions and regularly assess the impact of its regulatory activities to effectively manage risk and be efficient.

In order to protect investors and the public interest, the entire system of financial reporting, auditing, and regulation must be guided by the fundamental principles of having the right incentives to encourage key parties to do the right thing and adequate transparency to help ensure that the right things will happen, accompanied by full accountability. And the regulatory system must proactively assess and address risks within the system that threaten those fundamental principles.

The [Department of the Treasury's 2008 ACAP](#) report was an invaluable roadmap at a critical time in history for the PCAOB and the auditing profession. As the first comprehensive study of the profession since the 2002 legislation establishing the PCAOB, the report identifies many significant issues for the Board and the profession itself.

The PCAOB continues to focus on areas raised in the ACAP report. Those areas include promoting auditor objectivity and skepticism; expanding the auditor's report to provide useful information to investors; improving firm transparency reports, expanding the use and usefulness of audit quality indicators, continuing examination of auditor detection and prevention of fraud; and increasing coordination with foreign audit regulators in inspections, enforcement, standards and policy matters.

Since the time ACAP report was written, risks to audit quality have changed. In addition, new changes and innovations represent both opportunities and potential risks to audit quality. While key issues raised in the ACAP report remain relevant, audit firms and audit regulators must be insightful and forward-looking to detect new and emerging risks so that timely actions can be taken to ensure reliable, high quality auditing to support the capital markets and protect investors.

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## STANDING ADVISORY GROUP MEETING

### STATUS OF PCAOB-RELATED RECOMMENDATIONS FROM THE U.S. DEPARTMENT OF THE TREASURY'S ADVISORY COMMITTEE ON THE AUDITING PROFESSION

OCTOBER 13-14, 2010

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On October 6, 2008, the U.S. Department of Treasury's Advisory Committee on the Auditing Profession ("ACAP") issued its final report and recommendations to enhance the sustainability of a strong and vibrant public company auditing profession.<sup>1/</sup> A number of the recommendations involve the Public Company Accounting Oversight Board ("PCAOB" or "Board"). Below is a list of the formal recommendations – organized by area focus – that refer to or involve the PCAOB, as well as PCAOB developments on the implementation of those recommendations.<sup>2/</sup> In some cases, the explanatory text to

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<sup>1/</sup> U. S. Department of the Treasury, *Final Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury* ("ACAP Final Report") (October 6, 2008), available at: <http://www.treas.gov/offices/domestic-finance/acap/docs/final-report.pdf>.

<sup>2/</sup> Some of the recommendations affecting the PCAOB may also require certain action by the Securities and Exchange Commission ("SEC" or "Commission"). As a practical matter, the PCAOB consults with the SEC on policy level issues, such as those discussed in ACAP's Final Report. For its 2009 calendar year, the Board was required to consult with the Commission with respect to the implementation of the ACAP recommendations. See Order Approving Public Company Accounting Oversight Board Budget and Annual Accounting Support Fee for Calendar Year 2009, SEC Release 33-8989 (December 17, 2008).

This paper was developed by PCAOB staff to foster discussion among the members of the Standing Advisory Group. It is not a statement of the Board; nor does it necessarily reflect the views of the Board or staff.

these recommendations includes other suggested action for the PCAOB and, as appropriate, these suggestions are referred to in the update below.

### **Human Capital Recommendations**

**1. Recommendation 3. Ensure a sufficiently robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high quality audits. \* \* \* (b) Emphasize the utility and effectiveness of cross-sabbaticals.**

In connection with this recommendation, the ACAP recommended expanding faculty fellowship programs in agencies, such as those at the SEC and the Financial Accounting Standards Board ("FASB"), and making them available at the PCAOB.

On December 22, 2009, the PCAOB announced the establishment of and candidate solicitation for an Academic Fellow Program. This program is designed to appoint an experienced researcher and academic, with an active interest in auditing and oversight matters, to serve as an Academic Fellow for a term of up to 12 months.

The Academic Fellow is expected to provide analytical support and advice to the PCAOB's Office of Research and Analysis ("ORA") as well as other offices and divisions of the PCAOB and develop innovative ideas and problem-solving concepts within the framework of responsibilities of ORA. Such projects may include research on accounting and auditing matters, risk-assessment research, and/or other research and work relating to PCAOB activities.

On June 15, 2010, Acting Chairman Goelzer announced that Professor Michael Stein had been named as its inaugural fellow.<sup>3/</sup> Dr. Stein is assigned to ORA for the academic year 2010-2011.

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The PCAOB published a similar status report on the PCAOB-recommendations from the ACAP earlier this year. See [Status of PCAOB-Related Recommendations from the U.S. Department of Treasury's Advisory Committee on the Auditing Profession](#), PCAOB Staff Briefing Paper (April 7-8, 2010).

<sup>3/</sup> See [PCAOB Names Old Dominion University Professor Michael Stein as Inaugural Academic Fellow for 2010-2011](#), PCAOB Press Release (June 15, 2010).

Dr. Stein is a Professor of Accounting at Old Dominion University in Norfolk, Virginia. He has published articles in leading academic journals on topics such as: audit quality and audit market competitiveness; the pricing of litigation risk in audit fees; the measurement and identification of factors contributing to auditor productive efficiency; the estimation of auditors' materiality assessments; auditor changes and auditor tenure; and the measurement of the value of audits. He has completed multiple appointments as an editorial board member for *The Accounting Review* and *Contemporary Accounting Research* publications. He recently finished a term as an Associate Editor for the journal *Auditing: A Journal of Practice & Theory*.

### **Firm Structure and Finances Recommendations**

**2. Recommendation 1. Urge the Securities and Exchange Commission (SEC), and Congress as appropriate, to provide for the creation by the Public Company Accounting Oversight Board (PCAOB) of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.**

The PCAOB had discussions, on an informal basis, with various experts to solicit views on the potential scope, structure, and organization of a national center focused on the prevention and detection of financial fraud (the "Center").

Based on these discussions, the PCAOB developed a preliminary outline for the Center. The Center would (1) maintain a repository of information related to financial reporting fraud, including types of fraud, case histories and lessons learned, current trends and risks, and best practices to identify financial reporting fraud; (2) produce periodic and ad hoc reports on risks related to financial reporting; and (3) publish information to enhance understanding of the risk of financial fraud.

On April 6, 2010, the PCAOB posted to its Web site an announcement soliciting candidates for this director position.<sup>4/</sup>

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<sup>4/</sup> See [PCAOB Seeks Director, Financial Reporting Fraud Resource Center](#), PCAOB Press Release (April 6, 2010).

At the inaugural meeting of the Board's Investor Advisor Group ("IAG") on May 4, 2010, the Board sought input from its IAG on the establishment of a Center.<sup>5/</sup>

The Board is now in the process of interviewing candidates for the director of the Center. Once selected, the director, in consultation with the Board and PCAOB senior staff, will prepare an organizational plan and initial budget for the Center.

**3. Recommendation 2. Encourage greater regulatory cooperation and oversight of the public company auditing profession to improve the quality of the audit process and enhance confidence in the auditing profession and financial reporting. \* \* \* (b) Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.**

In connection with this recommendation, the Committee recommended mandating regular and formal roundtables of the PCAOB, the SEC, the Department of Justice, the state boards of accountancy, and the state attorneys general, to periodically review the overall enforcement regimes applicable to the public company auditing profession.

Coordination among regulators with jurisdiction over auditor conduct is also important to identify and address any regulatory gaps that could harm the investing public, and to provide for the most effective use of scarce regulatory resources. PCAOB enforcement staff already has regular informal and case-by-case contact with other enforcement agencies, as permitted by the Sarbanes-Oxley Act of 2002 ("Act"). The PCAOB is also considering whether a more formal meeting or meetings with appropriate enforcement agencies to discuss emerging risks in auditing, appropriate information-sharing, and other issues, would be useful in furtherance of the PCAOB's mission. In this regard, the PCAOB enforcement staff has met with SEC enforcement staff, with whom it closely coordinates its investigations, to discuss convening an appropriate first meeting based on these goals. The Board is hopeful that a first meeting will take place early in 2011.

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<sup>5/</sup> See [PCAOB Announces Inaugural Investor Advisory Group on May 4, 2010](#), PCAOB Press Release (April 20, 2010); See also [Investor Advisory Group of the Public Company Accounting Oversight Board: Summary of May 4, 2010 Meeting](#) at 1-3.

**4. Recommendation 3. Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze, explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.**

The Board has discussed this recommendation but has not taken any action.

Moreover, at the May 4, 2010 IAG meeting, the Board sought input from the IAG on the topic of greater transparency and governance of audit firms.<sup>6/</sup> Among the issues raised as part of this discussion was the use of firm advisory boards, composed of individuals who are independent from the audit firm.

**5. Recommendation 4. Urge the SEC to amend Form 8-K disclosure requirements to characterize appropriately and report every public company auditor change and to require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audit clients.**

The Board's inspection staff has obtained information regarding engagement partner changes on public company audits from certain auditing firms and, as appropriate, has utilized this information in its issuer engagement selection process.

**6. Recommendation 5: Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor's standard reporting model. Further, urge that the PCAOB and the SEC clarify in the auditor's report the auditor's role in detecting fraud under current auditing standards and further that the PCAOB periodically review and update these standards.**

- a. Consider Improvements to Auditor's Standard Reporting Model and Clarify in the Auditor's Report the Auditor's Role in Detecting Fraud

The Board discussed this recommendation with both its Standing Advisory Group ("SAG") and IAG.

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<sup>6/</sup> See Investor Advisory Group of the Public Company Accounting Oversight Board: Summary of May 4, 2010 Meeting at 5-6.



At the April 7-8, 2010 SAG meeting, panelists presented information relating to the history and evolution of the U.S. standard auditor's report and the ACAP recommendation. After the panelists' remarks, SAG members and observers discussed in break-out sessions potential ways to: (i) change the standard auditor's report and (ii) clarify in the auditor's report the auditor's role in detecting fraud. On the second day of the meeting, a summary of the break-out group discussions was presented to the SAG and SAG members had an opportunity to provide additional commentary.<sup>7/</sup>

At the May 4, 2010 IAG meeting, a panel discussion was held on greater transparency of the audit process.<sup>8/</sup> Among the topics discussed as part of this panel was the auditor's reporting model, including suggestions to clarify in the auditor's report the auditor's role in detecting fraud.

At the July 15, 2010 SAG meeting, the PCAOB's Office of the Chief Auditor updated and sought feedback from the SAG on potential next steps in the standard-setting process with respect to this issue.

Based on these discussions, the PCAOB has added a new project on the auditor's reporting model to its standard-setting agenda.<sup>9/</sup> The PCAOB's Office of the Chief Auditor is currently conducting research to ascertain and identify additional investor and user needs and plans to present its findings to the Board in the first quarter of 2011. The current standard-setting agenda contemplates that the Board will issue a related concept release in the second quarter of 2011 and hold a roundtable on the topic in the third quarter of 2011. This type of consultation with interested parties – through a roundtable, concept release and otherwise – is consistent with the part of the ACAP's Final Report on this recommendation that provides that "the PCAOB should consult with investors, other financial statement users, auditing firms, public companies,

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<sup>7/</sup> See ACAP Committee's Recommendation Relating to the Auditor's Reporting Model, PCAOB Standing Advisory Group, PCAOB Staff Briefing Paper (April 7-8, 2010).

<sup>8/</sup> See Investor Advisory Group of the Public Company Accounting Oversight Board: Summary of May 4, 2010 Meeting at 6-7.

<sup>9/</sup> See Office of the Chief Auditor Standard-Setting Agenda (October 2010).

academics, other market participants, and other state, federal, and foreign regulators."<sup>10/</sup>

b. Review and Update Auditing Standards Governing Fraud

One of the functions of the Board's Center on financial fraud will be to work collaboratively with the PCAOB's Office of the Chief Auditor as well as other divisions and offices to make recommendations to the Board as to whether auditing standards governing fraud detection and reporting should be changed.

The PCAOB also has several standard-setting projects on its agenda that address the assessment of fraud risk.<sup>11/</sup> Below are some developments in this area.

Risk Assessment Standards Integrating Auditor's Responsibility for Fraud: On August 5, 2010, the Board adopted eight auditing standards related to the auditor's assessment of and response to risk in an audit.<sup>12/</sup> Among other things, the standards integrate the auditor's responsibilities for considering fraud during the audit. This integration emphasizes that consideration of fraud is a central part of the audit process and should prompt auditors to make a more thoughtful and thorough assessment of fraud risks and develop appropriate audit responses. The standards also include additional requirements related to consideration of potential management bias in financial statements and fraud risks regarding omitted, incomplete, or inaccurate disclosures. The standards, if approved by the Commission, will become effective for audits of fiscal periods beginning on or after December 15, 2010.

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<sup>10/</sup> ACAP Final Report at VII:18.

<sup>11/</sup> See Office of the Chief Auditor Standard-Setting Agenda (October 2010).

<sup>12/</sup> See Auditing Standards related to the Auditor's Assessment of and Response to Risk and Related Amendments to PCAOB Standards, PCAOB Release No. 2010-004, PCAOB Rulemaking Docket Matter No. 026 (August 5, 2010). The Board has submitted final standards to the Commission for approval pursuant to Section 107 of the Act, which have been published in the Federal Register, 75 FR 59332 (September 27, 2010). The Commission comment period on these standards closes October 18, 2010.

The Board initially proposed these standards on October 21, 2008 and repropoed these standards on December 17, 2009.<sup>13/</sup> At the April 7-8, 2010 SAG meeting, the PCAOB's Office of the Chief Auditor provided a summary of the comments received on its repropoal.

Confirmation: On July 13, 2010, the Board propoed for public comment a new confirmation standard to supersede the PCAOB's existing confirmation standard.<sup>14/</sup> The propoed confirmation standard requires the auditor to perform confirmation procedures in response to significant risks, including fraud risks, and includes other procedures that address the risk of material misstatement due to error or fraud.

The comment period on the propoed standard closed on September 13, 2010. The Board received 26 comments and is considering the comments received. At the October 13-14, 2010 SAG meeting, the PCAOB's Office of the Chief Auditor will provide a summary of the comments received.

Related Parties: Among the priorities on the Board's standard-setting agenda is a project on related party transactions, which can be a contributing factor in financial reporting frauds. At its October 14-15, 2009 meeting, the SAG discussed certain matters in connection with the development of the Board's standard-setting project on

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<sup>13/</sup> See Propoed Auditing Standards related to the Auditor's Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards, PCAOB Release No. 2008-006, PCAOB Rulemaking Docket Matter No. 026 (October 21, 2008) and Propoed Auditing Standards related to the Auditor's Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards, PCAOB Release No. 2009-007, PCAOB Rulemaking Docket Matter No. 026 (December 17, 2009).

<sup>14/</sup> See Propoed Auditing Standard Related to Confirmations and Related Amendments to PCAOB Standards, PCAOB Release No. 2010-003, PCAOB Rulemaking Docket Matter No. 028 (July 13, 2010). On April 14, 2009, the Board issued for public comment a concept release on the potential direction of a propoed standards-setting project on audit confirmations. See Concept Release on Possible Revisions to the PCAOB's Standard on Audit Confirmations, PCAOB Release No. 2009-002, PCAOB Rulemaking Docket Matter No. 028 (April 14, 2009).

related parties.<sup>15/</sup> Based on this input, the Board is evaluating potential revisions to the related parties auditing standard and plans to issue a proposed standard in 2011.

Audit Practice Alerts: In addition to its standard-setting, the PCAOB uses Staff Audit Practice Alerts to highlight new, emerging, or otherwise noteworthy circumstances – including fraud risks – that may affect how auditors conduct audits under the existing requirements of PCAOB standards and relevant laws. For example, Staff Audit Practice Alert No. 3, *Audit Considerations in the Current Economic Environment* relates to auditing challenges as a result of the economic crisis and highlights certain fraud risks.<sup>16/</sup> Moreover, on April 7, 2010, the PCAOB issued Staff Audit Practice Alert No. 5, *Auditor Considerations Regarding Significant Unusual Transactions*, relating to significant unusual transactions that can provide opportunities for companies to engage in fraudulent financial reporting.<sup>17/</sup>

**7. Recommendation 6: Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report.**

At the October 22-23, 2008 SAG meeting, a panel consisting of an investor, an academic, and a representative from a large accounting firm, discussed whether the PCAOB should consider mandating the engagement partner's signature on the auditor's report.<sup>18/</sup>

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<sup>15/</sup> See Related Parties, PCAOB Standing Advisory Group Meeting, PCAOB Staff Briefing Paper (October 14-15, 2009).

<sup>16/</sup> See Staff Audit Practice Alert No. 3, *Audit Considerations in the Current Economic Environment*, PCAOB Staff Audit Practice Alert (December 5, 2008).

<sup>17/</sup> See Staff Audit Practice Alert No. 5, *Auditor Considerations Regarding Significant Unusual Transactions*, PCAOB Staff Audit Practice Alert (April 7, 2010).

<sup>18/</sup> See Panel Discussion – Signing the Auditor's Report, PCAOB Standing Advisory Group Meeting, PCAOB Staff Briefing Paper (October 22-23, 2008).

On July 28, 2009, the Board issued a concept release to solicit comment on whether the engagement partner should be required to sign the audit report.<sup>19/</sup> The concept release briefly discusses views on this issue from the SAG and ACAP and provides some background on signature requirements in Europe. The release also discusses reasons for a signature requirement and potential amendments to PCAOB standards.

The deadline for comments on the concept release was September 11, 2009. The Board received 23 comment letters. At the October 14-15, 2009 SAG meeting, the PCAOB's Office of the Chief Auditor provided an update on the concept release and comments received.

At the May 4, 2010 IAG meeting, the Board sought input from the IAG on the topic of greater transparency and governance of audit firms.<sup>20/</sup> Among the issues discussed was mandating the engagement partner's signature on the auditor's report.

The Board's consideration of next steps is pending further action.

**8. Recommendation 7. Urge the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating (a) information required by the EU's Eighth Directive, Article 40 Transparency Report deemed appropriate by the PCAOB, and (b) such key indicators of audit quality and effectiveness as determined by the PCAOB in accordance with Recommendation 3 in Chapter VIII of this Report. Further, urge the PCAOB to require that, beginning in 2011, the larger auditing firms file with the PCAOB on a confidential basis audited financial statements.**

The Board has discussed this recommendation but has not taken any action.

At the May 4, 2010 IAG meeting, the Board sought input from the IAG on the topic of greater transparency and governance of audit firms.<sup>21/</sup> Among the issues raised as part of this discussion was the disclosures of "audit quality indicators".

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<sup>19/</sup> See Concept Release on Requiring the Engagement Partner to Sign the Audit Report, PCAOB Release No. 2009-005 (July 28, 2009).

<sup>20/</sup> See Investor Advisory Group of the Public Company Accounting Oversight Board: Summary of May 4, 2010 Meeting at 5-6.

## **Concentration and Competition Recommendations**

**9. Recommendation 1. Reduce barriers to the growth of smaller auditing firms consistent with an overall policy goal of promoting audit quality. Because smaller auditing firms are likely to become significant competitors in the market for larger company audits only in the long term, the Committee recognizes that Recommendation 2 will be a higher priority in the near term. \* \* \* (b) Include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements.**

In connection with this recommendation, the ACAP Final Report also notes that "the PCAOB should inquire about whether the transition process [between predecessor and successor auditors] was cooperative and transparent," when the PCAOB interviews the audit committee chair in connection with an inspection of an audit engagement at a company that has undergone a change of auditors.<sup>22/</sup>

The PCAOB's Division of Registration and Inspections has asked certain firms about the cooperativeness and transparency of the transition process between predecessor and successor auditors in its interviews of audit committee chairs that have undergone a change in auditors.

With respect to the recommendation relating to including smaller audit firm representatives in committees, public forums, fellowships, and other engagements, the PCAOB has several initiatives.

First, the Board hosts the Forums on Auditing in the Small Business Environment. Each year, since the first forum was held at the end of 2004, the PCAOB has held between six and ten of these forums in locations around the United States to educate auditors of smaller public companies about the work of the Board, specifically the PCAOB inspection process and the impact of new auditing standards. Most recently, seven forums were held in 2008 and six forums were held in 2009; 658

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<sup>21/</sup> See Investor Advisory Group of the Public Company Accounting Oversight Board: Summary of May 4, 2010 Meeting at 5-6.

<sup>22/</sup> ACAP Final Report at VIII:5.



auditors attended the seven forums in 2008, and 590 auditors attended the six forums in 2009.

Seven forums have been scheduled for 2010; five forums have taken place and forums in Dallas, Texas and Miami, Florida are scheduled to be held on November 2, 2010 and December 1, 2010, respectively.<sup>23/</sup> Attendance at the forums is limited to smaller auditing firms registered with the PCAOB. The forums are intended to give these firms an opportunity to meet directly with the PCAOB Board members and staff and gain insight with respect to the PCAOB's inspection process and its standard-setting work.

Moreover, the PCAOB includes representatives of smaller audit firms on its SAG, as well as on panels discussing certain issues with the SAG, to obtain input on standard-setting projects from auditors with this perspective.

In addition, representatives of smaller audit firms are often consulted on an ad hoc basis with respect to certain standard-setting projects. For example, representatives from smaller auditing firms assisted the PCAOB's Office of the Chief Auditor in developing staff guidance on auditing internal control over financial reporting in smaller public companies.<sup>24/</sup>

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") vested the PCAOB with the authority to oversee auditors of the financial statements and selected practices and procedures of all SEC-registered securities broker-dealers. The great majority of the more than 500 additional firms that have registered with the Board because they perform broker-dealer audits are, like their clients, small businesses. In light of this new authority, the Board began to reassess its communications and outreach strategy, particularly with respect to entities in the small business community. As part of this effort, in 2011, the Board intends to develop a new forum focused on audits of practices, procedures and financial statements of broker-dealers.

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<sup>23/</sup> For a schedule of the 2010 PCAOB Forums on Auditing in the Small Business Environment, see <http://pcaobus.org/Featured/Pages/SmallBusinessForums.aspx>.

<sup>24/</sup> See [An Audit of Internal Control over Financial Reporting that is Integrated with an Audit of Financial Statements – Guidance for Auditors of Smaller Public Companies](#), Staff Views (January 23, 2009).

**10. Recommendation 2. Monitor potential sources of catastrophic risk faced by public company auditing firms and create a mechanism for the preservation and rehabilitation of troubled larger public company auditing firms. \* \* \* (a) As part of its current oversight over registered auditing firms, the PCAOB should monitor potential sources of catastrophic risk which would threaten audit quality.**

The Board has discussed this recommendation but has not taken any action.

As part of its annual inspections of the largest firms, however, the PCAOB reviews pending litigation and discusses the firms' current evaluation of the likelihood of incurring significant litigation losses or costs. The PCAOB also inspects the firms' quality control systems, since catastrophic risk could stem from failures in these systems, including the manner in which these systems are applied to particular issuer audits. The relevant inspection procedures in this area include: (i) reviewing how the firm reacts to restatements or other potential quality control defects once known, such as internal inspection findings; (ii) evaluating a firm's client acceptance and retention procedures to ensure the firm accepts reputable clients for which the firm has appropriate and knowledgeable resources to provide the audit services; and (iii) considering the level of quality controls that exist over non-U.S. associates of the firm that participate in the audits conducted by the U.S. firm when auditing multi-national issuers.

At the May 4, 2010 IAG meeting, the Board sought input from the IAG on the topic of greater transparency and governance of audit firms.<sup>25/</sup> In this context, some IAG members discussed catastrophic or systemic risk to auditing firms.

**11. Recommendation 3. Recommend the PCAOB, in consultation with auditors, investors, public companies, audit committees, boards of directors, academics, and others, determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.**

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<sup>25/</sup> See Investor Advisory Group of the Public Company Accounting Oversight Board: Summary of May 4, 2010 Meeting at 5-6.

At its October 22-23, 2008 meeting, the SAG discussed this recommendation.<sup>26/</sup> Specifically, panelists provided background information on audit quality, including an overview of the ACAP recommendation, a review of selected academic research on audit quality, and key points from initiatives on audit quality by the UK Financial Reporting Council and the Transparency Report required by the EU's Eighth Directive. SAG members, as a group and in three break-out sessions, then discussed issues regarding the feasibility of developing such indicators.

The PCAOB's Office of the Chief Auditor is also monitoring work in this area by others, such as International Organization of Securities Commissions ("IOSCO") and the International Auditing and Assurance Standards Board ("IAASB").<sup>27/</sup>

In addition, at the May 4, 2010 IAG meeting, the Board sought input from the IAG on the topic of greater transparency and governance of audit firms.<sup>28/</sup> Among the issues raised as part of this discussion was the disclosures of "audit quality indicators".

**12. Recommendation 4. Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.**

**(a) Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible. The American Institute of Certified Public Accountants (AICPA) and state boards of accountancy should clarify and prominently note that differences exist between the SEC and PCAOB standards (applicable to public companies) and the AICPA and state standards**

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<sup>26/</sup> See SAG Discussion – Treasury Advisory Committee's Recommendation Relating to the Feasibility of Developing Key Indicators of Audit Quality and Effectiveness, PCAOB Standing Advisory Group, PCAOB Staff Briefing Paper (October 22-23, 2008).

<sup>27/</sup> See e.g. Transparency of Firms that Audit Public Companies, Consultation Report, Technical Committee of the International Organization of Securities Commissions (September 2009).

<sup>28/</sup> See Investor Advisory Group of the Public Company Accounting Oversight Board: Summary of May 4, 2010 Meeting at 5-6.

**(applicable in all circumstances, but subject to SEC and PCAOB standards, in the case of public companies) and indicate, at each place in their standards where differences exist, that stricter SEC and PCAOB independence requirements applicable to public company auditors may supersede or supplement the stated requirements. This compilation should not require rulemaking by either the SEC or the PCAOB because it only calls for assembly and compilation of existing rules.**

**(b) Develop training materials to help foster and maintain the application of healthy professional skepticism with respect to issues of independence and other conflicts among public company auditors, and inspect auditing firms, through the PCAOB inspection process, for independence training of partners and mid-career professionals.**

With respect to compiling and publishing the SEC's and PCAOB's independence requirements into a single document, the PCAOB has assisted the SEC with respect to this compilation, particularly as it relates to PCAOB's independence requirements.

With respect to fostering professional skepticism, inherent within the PCAOB inspection process is an evaluation of a firm's application of professional skepticism. As part of that evaluation, the inspection staff routinely evaluates the development of processes by the firms designed to improve the application of professional skepticism. Examples of the processes developed by firms include additional levels of review, increased involvement of specialists, additional guidance, and training.

**13. Recommendation 6. Enhance regulatory collaboration and coordination between the PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the United States.**

The PCAOB engages in dialogue with its non-U.S. counterparts on a bilateral basis to facilitate joint inspections or PCAOB-only inspections of non-U.S. accounting firms registered with the PCAOB. Over 900 non-U.S. accounting firms, located in 87 countries, are registered with the PCAOB. Since its inception, the Board has conducted 252 inspections of non-U.S. firms located in 34 jurisdictions. Of these 252 inspections, 103 were conducted jointly with a non-U.S. oversight body.

Moreover, while the Board would like to further its cooperation and coordination with all of its non-U.S. counterparts and has tried for several years to negotiate arrangements with authorities in the affected jurisdictions to eliminate asserted

obstacles to Board inspections, obstacles persist in several jurisdictions. In some of those jurisdictions, there have been recent indications of progress.<sup>29/</sup> The Board continues to try to work through the issues with the relevant foreign authorities. Currently, however, in some jurisdictions, there is substantial uncertainty about whether and when PCAOB inspections of registered firms will be able to go forward.

The PCAOB also participates as a member in the International Forum of Independent Audit Regulators ("IFIAR"), whose purpose is to bring public auditor oversight entities together to share information and exchange ideas. Currently, there are 37 countries represented among the IFIAR members. Since the PCAOB joined IFIAR in 2006, the PCAOB has participated in eight IFIAR plenary meetings and four IFIAR inspection workshops. The PCAOB will host the next IFIAR inspection workshop in Washington D.C. in early 2011.

The PCAOB hosts an International Auditor Regulatory Institute in Washington D.C. In October 2009, the PCAOB held its third annual International Auditor Regulatory Institute ("Institute"). Representatives of auditor oversight bodies and government agencies from more than 42 countries participated to learn more about the PCAOB's programs and exchange views on issues that have an impact on the oversight of auditors.

The Institute offered seminars on the structure of the PCAOB's auditor oversight program, considerations relevant to international inspections, and current topics in enforcement and standard setting. The Institute also included a panel discussion with representatives of several of the PCAOB's international counterparts, addressing a range of issues related to auditor oversight worldwide.

The PCAOB plans to host its fourth annual Institute in Washington D.C. in November 2010.

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<sup>29/</sup> On September 1, 2010, the European Commission adopted a decision recognizing the "adequacy" of the PCAOB for purposes of the European Union's Statutory Audit Directive. This decision permits the individual Member State audit regulators to enter into bilateral arrangements with the PCAOB, subject to certain conditions. The PCAOB is currently negotiating with several EU audit regulators and hopes to resolve the remaining obstacles to inspections.



Status of PCAOB-Related  
Recommendations from the U.S.  
Department of the Treasury's Advisory  
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The PCAOB is a private-sector, non-profit corporation that oversees the auditors of public companies and brokers and dealers in order to protect the interests of investors and further the public interest in the preparation of informative, fair, and independent audit reports.



Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession

June 27, 2016

Mr. James R. Doty  
Chairman  
Public Company Accounting Oversight Board  
1666 K Street NW  
Washington, DC 20006

Dear Chairman Doty:

In 2007 the U.S. Secretary of the Treasury, the Honorable Henry M. Paulson, Jr., announced and appointed an Advisory Committee on the Auditing Profession (ACAP) "...to consider and develop recommendations relating to the sustainability of the auditing profession." Secretary Paulson appointed twenty one members to the Committee, with a variety of backgrounds including business executives and corporate board members, former Securities and Exchange Commission (SEC) and Federal Reserve Chairmen, former SEC chief accountants, auditors, investors and attorneys. The Public Company Accounting Oversight Board (PCAOB) Chairman served as an observer to the Committee. A year later in October 2008, the ACAP issued its recommendations.

The PCAOB Investor Advisory Group (IAG) has benefited, as we hope the PCAOB board members and staff have, from the discussions at the IAG meetings in past years. We again look forward to our next meeting on October 27, 2016. At that meeting, a working group of the IAG will be making a presentation to the members of the PCAOB with respect to the progress that has been made in the intervening eight years, on the recommendations of the ACAP. Accordingly, the working group is diligently undertaking to identify the actions taken to date by each entity to which the recommendations were addressed, as well as what obstacles, if any, they have faced in addressing the ACAP recommendations.

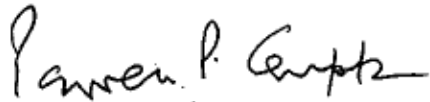
To that end, the working group would appreciate it if the PCAOB or its staff, could provide a response to the working group, with respect to the ACAP recommendations to the PCAOB in the attached Appendix A, which have been highlighted. (A similar request is being sent to each entity that the ACAP directed its recommendations to.) In particular, if the response could set forth the steps or actions taken to address and implement the recommendations, and when they were taken, would be most useful. This would include either interim or final actions. Such a response would be helpful in ensuring our report to the PCAOB is as comprehensive as possible. In order to adequately consider the response,

it would be appreciated if it could be received by no later than September 15, 2016. You can address it to the working group co-chair. Parveen Gupta, Lehigh University, 621 Taylor Street, College of Business and Economics, Lehigh University, Bethlehem PA, 18015. Please do not hesitate to Call Mr. Gupta (610-758-3443) or Mr. Turner (303-956-4895) if you have any questions.

This project is being undertaken by the IAG working group and its members. As such, it is not a project being undertaken by the PCAOB or its staff. However, we hope it will result in a report that is informative and helpful to the PCAOB in its endeavors.

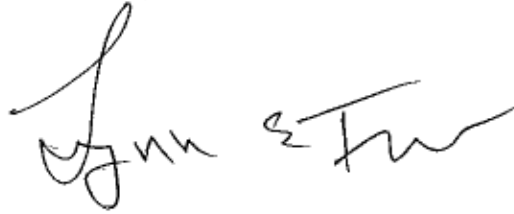
Again, we greatly appreciate your support and participation at previous IAG meetings.

Sincerely,



Parveen Gupta

Investor Advisory Group  
Working Committee Co-Chair



Lynn Turner

Investor Advisory Group  
Working Committee Co-Chair

## APPENDIX A

### U.S. Treasury Advisory Committee on the Auditing Profession

October, 2008 Report

Recommendations made to the Securities and Exchange Commission and Others

### Advisory Committee on the Auditing Profession Final Report

#### Human Capital Recommendations

**Recommendation 1.** Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high quality audits.

(a) Regularly update the accounting certification examinations to reflect changes in the accounting profession, its relevant professional and ethical standards, and the skills and knowledge required to serve increasingly global capital markets.

(b) Reflect real world changes in the business environment more rapidly in teaching materials.

(c) Require that schools build into accounting curricula current market developments.

**Recommendation 2.** Improve the representation and retention of minorities in the auditing profession so as to enrich the pool of human capital in the profession.

(a) Recruit minorities into the auditing profession from other disciplines and careers.

(b) Institute initiatives to increase the retention of minorities in the profession.

(c) Emphasize the role of community colleges in the recruitment of minorities into the auditing profession.

(d) Emphasize the utility and effectiveness of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.

(e) Increase the numbers of minority accounting doctorates through focused efforts.

**Recommendation 3.** Ensure a sufficiently robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high quality audits.

(a) Increase the supply of accounting faculty through public and private funding and raise the number of professionally qualified faculty that teach on campuses.

(b) Emphasize the utility and effectiveness of cross-sabbaticals.

(c) Create a variety of tangible and sufficiently attractive incentives that will motivate private sector institutions to fund both accounting faculty and faculty research, to provide practice materials for academic research and for participation of professionals in behavioral and field study projects, and to encourage practicing accountants to pursue careers as academically and professionally qualified faculty.

**Recommendation 4.** Develop and maintain consistent demographic and higher education program profile data.

**Recommendation 5.** Encourage the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession.

#### **Firm Structure and Finances Recommendations**

✓ **Recommendation 1.** Urge the Securities and Exchange Commission (SEC), and Congress as appropriate, to provide for the creation by the Public Company Accounting Oversight Board (PCAOB) of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.

**Recommendation 2.** Encourage greater regulatory cooperation and oversight of the public company auditing profession to improve the quality of the audit process and enhance confidence in the auditing profession and financial reporting.

(a) Institute the following mechanism to encourage the states to substantially adopt the mobility provisions of the Uniform Accountancy Act, Fifth Edition (UAA): If states have failed to adopt the mobility provisions of the UAA by December 31, 2010, Congress should pass a federal provision requiring those states to adopt these provisions.

✓ (b) Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.

(c) Urge the states to create greater financial and operational independence of their state boards of accountancy.

✓ Recommendation 3. Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze, explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.

✓ Recommendation 4. Urge the SEC to amend Form 8-K disclosure requirements to characterize appropriately and report every public company auditor change and to require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audit clients.

✓ Recommendation 5. Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor's standard reporting model. Further, urge that the PCAOB and the SEC clarify in the auditor's report the auditor's role in detecting fraud under current auditing standards and further that the PCAOB periodically review and update these standards.

✓ Recommendation 6. Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report.

✓ Recommendation 7. Urge the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating (a) information required by the EU's Eighth Directive, Article 40 Transparency Report deemed appropriate by the PCAOB, and (b) such key indicators of audit quality and effectiveness as determined by the PCAOB in accordance with Recommendation 3 in Chapter VIII [Concentration and Competition] of this Report. Further, urge the PCAOB to require that, beginning in 2011, the larger auditing firms file with the PCAOB on a confidential basis audited financial statements.

## **Concentration and Competition Recommendations**

**Recommendation 1.** Reduce barriers to the growth of smaller auditing firms consistent with an overall policy goal of promoting audit quality. Because smaller auditing firms are likely to become significant competitors in the market for larger company audits only in the long term, the Committee recognizes that Recommendation 2 will be a higher priority in the near term.

(a) Require disclosure by public companies in their registration statements, annual reports, and proxy statements of any provisions in agreements with third parties that limit auditor choice.

✓ (b) Include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements.

✓ **Recommendation 2.** Monitor potential sources of catastrophic risk faced by public company auditing firms and create a mechanism for the preservation and rehabilitation of troubled larger public company auditing firms.

✓ (a) As part of its current oversight over registered auditing firms, the PCAOB should monitor potential sources of catastrophic risk which would threaten audit quality.

✓ (b) Establish a mechanism to assist in the preservation and rehabilitation of a troubled larger auditing firm. A first step would encourage larger auditing firms to adopt voluntarily a contingent streamlined internal governance mechanism that could be triggered in the event of threatening circumstances. If the governance mechanism failed to stabilize the firm, a second step would permit the SEC to appoint a court-approved trustee to seek to preserve and rehabilitate the firm by addressing the threatening situation, including through a reorganization, or if such a step were unsuccessful, to pursue an orderly transition.

✓ **Recommendation 3.** Recommend the PCAOB, in consultation with auditors, investors, public companies, audit committees, boards of directors, academics, and others, determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.

✓ **Recommendation 4.** Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit



committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.

- ✓ (a) Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible. The AICPA and state boards of accountancy should clarify and prominently note that differences exist between the SEC and PCAOB standards (applicable to public companies) and the AICPA and state standards (applicable in all circumstances, but subject to SEC and PCAOB standards, in the case of public companies) and indicate, at each place in their standards where differences exist, that stricter SEC and PCAOB independence requirements applicable to public company auditors may supersede or supplement the stated requirements. This compilation should not require rulemaking by either the SEC or the PCAOB because it only calls for assembly and compilation of existing rules.
- ✓ (b) Develop training materials to help foster and maintain the application of healthy professional skepticism with respect to issues of independence and other conflicts among public company auditors, and inspect auditing firms, through the PCAOB inspection process, for independence training of partners and mid-career professionals.

**Recommendation 5.** Adopt annual shareholder ratification of public company auditors by all public companies.

- ✓ **Recommendation 6.** Enhance regulatory collaboration and coordination between the PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the United States.

# 5

## **United States Securities and Exchange Commission**



OFFICE OF THE  
CHIEF ACCOUNTANT

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

October 13, 2016

Dr. Parveen Gupta  
Mr. Lynn E. Turner  
Working Committee Co-Chairs  
Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory Committee on the Auditing Profession

Dear Dr. Gupta and Mr. Turner:

This letter responds to your June 27, 2016 letter to Securities and Exchange Commission ("SEC") Chair Mary Jo White regarding the work of the Advisory Committee on the Auditing Profession ("ACAP") and the report it issued in 2008.<sup>1</sup>

As I mentioned when we spoke recently, I strongly share the working group members' interest in the sustainability of a strong and vibrant auditing profession. The credibility of financial reporting depends on thorough audits performed by independent auditors. I believe audit quality has improved during the close to 15 years since the passage of the Sarbanes-Oxley Act of 2002 and the creation of the Public Company Accounting Oversight Board ("PCAOB"), which is responsible for overseeing the audits and auditors of public companies and SEC registered broker-dealers. However, the hard work of the PCAOB and others in the auditing profession continues, as is reflected in their robust and ongoing standard setting agendas.

I also believe that the design of the PCAOB's inspections program, the focus on the importance of the audit committee's oversight role, and the improvement in the transparency of drivers of audit quality have all contributed to the improvements in audit quality. I believe it is very important for this positive momentum to continue to keep pace with investor expectations as well as new and emerging financial reporting risks. It is thus incumbent upon us to continue to monitor the current environment to identify and understand the issues to be addressed as well as the range of potential approaches to addressing those issues.

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<sup>1</sup> See *Advisory Committee on the Auditing Profession Final Report* (Oct. 6, 2008), available at <https://www.treasury.gov/about/organizational-structure/offices/Documents/final-report.pdf> (the "Final Report").

I understand that the PCAOB has separately provided a response to you on the connections between their activities and the ACAP recommendations. I will not repeat the matters addressed in their response.

The Final Report included recommendations organized according to the areas of study of the three subcommittees. The following is a summary of the various actions taken to date based on the SEC agenda and priorities, which also address to some extent the matters identified in the recommendations.<sup>2</sup>

### Firm Structure and Finances

One of the recommendations encourages greater regulatory cooperation and oversight of the public company auditing profession. The objective of our cooperation and frequent dialogue with the PCAOB is to assess whether more should and could be done in our oversight of auditors. Among the regulatory activities we engage in, the SEC staff and the PCAOB staff foster robust cooperation, engage with co-extensive enforcement authority over auditors, and meet formally on a quarterly basis and more frequently on routine oversight and standard setting activities. The SEC Division of Enforcement's Financial Reporting and Auditing ("FRAud") Group focuses on financial reporting and audit failures, and the Division also has its "Operation Broken Gate" initiative to identify auditors who neglect their duties and the auditing standards. Recent examples of SEC auditor enforcement efforts, in close coordination with the PCAOB, include charges against two national firms and associated partners for deficient audits<sup>3</sup> and numerous sanctions of other firms stemming from Operation Broken Gate.<sup>4</sup>

Also, the SEC and the PCAOB are involved with the International Forum of Independent Audit Regulators ("IFIAR"), which brings together independent audit regulators from 51 jurisdictions to collaborate on regulatory activity. Committee 1 of International Organization of Securities Commissions' ("IOSCO"), which the SEC is a member of, represents IOSCO as an observer at meetings of IFIAR. The PCAOB participates and has an active leadership role in IFIAR. Additionally, the Financial Stability Board ("FSB"), which brings together senior policy makers from G20 countries, has held roundtables on effective audit regulation and oversight.

As it relates to improving the transparency of audit firms, IOSCO's Committee 1 led the effort to recently publish a "Statement on Transparency of Firms that Audit Public Companies" by IOSCO to promote good practice and contribute to high quality audit firm transparency reports.<sup>5</sup> That Committee was chaired by a senior member of OCA. Additionally, I am aware of and support and encourage the current efforts certain audit firms are making to improve

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<sup>2</sup> The five human capital recommendations are omitted from this document as they do not suggest significant actions by the SEC or PCAOB beyond expanding faculty fellowship programs at the SEC and PCAOB. See Section VI of the Final Report. The subheadings reflect Sections VII and VIII of the Final Report.

<sup>3</sup> See, e.g., <https://www.sec.gov/news/pressrelease/2015-184.html> and <https://www.sec.gov/news/pressrelease/2015-272.html>.

<sup>4</sup> See, e.g., <https://www.sec.gov/News/PressRelease/Detail/PressRelease/1370543281121>.

<sup>5</sup> IOSCO Final Report: *Statement on Transparency of Firms that Audit Public Companies* (Nov. 2015), available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD511.pdf>.

transparency in their reporting with respect to matters such as firm governance and the system of quality control for their financial statement audits.

As it relates to governance matters, the SEC issued a concept release in July 2015 seeking public comment regarding audit committee reporting requirements, including potential disclosure requirements regarding shareholder ratification and audit committee input in selecting the engagement partner, among many other important matters.<sup>6</sup> The SEC staff is currently reviewing and analyzing over 100 comment letters received in response to the concept release and monitoring any voluntary changes from the awareness brought to the issues to determine potential next steps to propose to the Commission for consideration. It is also relevant to note that SEC Form 8-K, item 4.01, requires disclosure of changes in a registrant's audit firm.

### Concentration and Competition

In the context of reducing any barriers to competition for smaller audit firms, the Final Report included a recommendation to require disclosure by registrants of provisions in agreements that limit auditor choice. While registrants must disclose information about material definitive agreements, those disclosure requirements do not generally specify disclosures regarding provisions within agreements that limit auditor choice. The audit committee concept release previously mentioned solicits feedback regarding possible disclosure of factors considered by the audit committee when selecting or retaining the auditor, which could include information about consideration of smaller audit firms. As mentioned previously, the release also discusses potential additional disclosures related to the ratification by shareholders of the selection of the independent auditor.

Also, SEC staff in the Office of the Chief Accountant has encouraged applicants from firms of all sizes to apply to our professional accounting fellowship programs. Successful applicants have included former employees from small and mid-size firms. The office also utilizes professionals from other regulators and other SEC offices and divisions on a time limited basis to further provide the multi-disciplinary talent needed for today's priorities.

Finally, as it relates to promoting an understanding and compliance with auditor independence requirements, the SEC staff continues to emphasize the importance of the independence requirements through speeches,<sup>7</sup> forums, and other public venues. In addition, staff within the SEC Division of Enforcement has been active in bringing cases against auditors who violate independence rules. As an example, the SEC recently brought two cases against a large firm and three former partners for auditor independence failures due to inappropriately close personal relationships.<sup>8</sup>

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<sup>6</sup> See *Possible Revisions to Audit Committee Disclosures*, Release No. 33-9862 (Jul. 1, 2015) [80 FR 38995], available at <https://www.sec.gov/rules/concept/2015/33-9862.pdf>.

<sup>7</sup> See, e.g., Wesley R. Bricker, Interim Chief Accountant, *Remarks before the AICPA National Conference on Banks and Savings Institutions* (Sept. 21, 2016), available at <https://www.sec.gov/news/speech/bricker-remarks-aicpa-national-conf-banks-savings-institutions.html> and Wesley R. Bricker, Deputy Chief Accountant, *Remarks before the 35th Annual SEC and Financial Reporting Institute Conference* (Jun. 9, 2016), available at <https://www.sec.gov/news/speech/bricker-remarks-35th-financial-reporting-institute-conference.html>.

<sup>8</sup> See, e.g., <https://www.sec.gov/news/pressrelease/2016-187.html>.

I hope you and the other members of the PCAOB Investor Advisory Group find these examples helpful as you continue to contribute your thought leadership to the important work of the PCAOB. I would be pleased to make myself and my staff available to discuss these matters further as needed. I look forward to participating in the dialogue at the IAG meeting. Please feel free to contact me directly at 202-551-3014.

Sincerely,

A handwritten signature in black ink, appearing to be 'Wes Bricker', with a long horizontal line extending to the right.

Wes Bricker  
Interim Chief Accountant



Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession

June 27, 2016

Mary Jo White  
Chairman  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Dear Chairman White:

In 2007 the U.S. Secretary of the Treasury, the Honorable Henry M. Paulson, Jr., announced and appointed an Advisory Committee on the Auditing Profession (ACAP) "...to consider and develop recommendations relating to the sustainability of the auditing profession." Secretary Paulson appointed twenty one members to the Committee, with a variety of backgrounds including business executives and corporate board members, former Securities and Exchange Commission (SEC) and Federal Reserve Chairmen, former SEC chief accountants, auditors, investors and attorneys. The SEC had two observers to the Committee. A year later in October 2008, the ACAP issued its recommendations.

The PCAOB Investor Advisory Group has benefited by your participation in its meetings in past years. We again look forward to the participation of the SEC in our next meeting on October 27, 2016. At that meeting, a working group of the IAG will be making a presentation to the members of the Public Company Accounting Oversight Board (PCAOB) with respect to the progress that has been made in the intervening eight years, on the recommendations of the ACAP. Accordingly, the working group is diligently undertaking to determine to identify the actions taken to date by each entity to which the recommendations were addressed, as well as what obstacles, if any, they have faced in addressing the ACAP recommendations.

To that end, the working group would appreciate it if the SEC or its staff, could provide a response to the working group, with respect to the ACAP recommendations to the SEC in the attached Appendix A, which have been highlighted. (A similar request is being sent to each entity that the ACAP directed its recommendations to.) In particular, if the response could set forth the steps or actions taken to address and implement the recommendations, and when they were taken, would be most useful. This would include either interim or final actions. Such a response would be helpful in ensuring our report to the PCAOB is as comprehensive as possible. In order to adequately consider the response, it would be

appreciated if it could be received by no later than September 15, 2016. You can address it to the working group co-chair, Parveen Gupta, Lehigh University, 621 Taylor Street, College of Business and Economics, Lehigh University, Bethlehem PA, 18015. Please do not hesitate to Call Mr. Gupta (610-758-3443) or Mr. Turner (303-956-4895) if you have any questions.

This project is being undertaken by the IAG working group and its members. As such, it is not a project being undertaken by the PCAOB or its staff. However, we hope it will result in a report that is informative and helpful to the PCAOB in its endeavors.

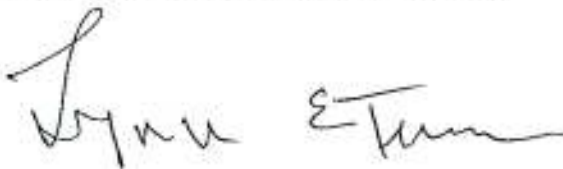
Again, we greatly appreciate your support and participation at previous IAG meetings.

Sincerely,



Parveen Gupta

Investor Advisory Group  
Working Committee Co-Chair



Lynn E. Turner

Investor Advisory Group  
Working Committee Co-Chair

Cc: Kara M. Stein - Commissioner  
Michael S. Piwowar - Commissioner  
James Schnurr - Chief Accountant

## APPENDIX A

### U.S. Treasury Advisory Committee on the Auditing Profession

October, 2008 Report

Recommendations made to the Securities and Exchange Commission and Others

### Advisory Committee on the Auditing Profession Final Report

#### Human Capital Recommendations

**Recommendation 1.** Implement market-driven, dynamic curricula and content for accounting students that continuously evolve to meet the needs of the auditing profession and help prepare new entrants to the profession to perform high quality audits.

(a) Regularly update the accounting certification examinations to reflect changes in the accounting profession, its relevant professional and ethical standards, and the skills and knowledge required to serve increasingly global capital markets.

(b) Reflect real world changes in the business environment more rapidly in teaching materials.

(c) Require that schools build into accounting curricula current market developments.

**Recommendation 2.** Improve the representation and retention of minorities in the auditing profession so as to enrich the pool of human capital in the profession.

(a) Recruit minorities into the auditing profession from other disciplines and careers.

(b) Institute initiatives to increase the retention of minorities in the profession.

(c) Emphasize the role of community colleges in the recruitment of minorities into the auditing profession.

(d) Emphasize the utility and effectiveness of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.

(e) Increase the numbers of minority accounting doctorates through focused efforts.



**Recommendation 3.** Ensure a sufficiently robust supply of qualified accounting faculty to meet demand for the future and help prepare new entrants to the profession to perform high quality audits.

(a) Increase the supply of accounting faculty through public and private funding and raise the number of professionally qualified faculty that teach on campuses.

(b) Emphasize the utility and effectiveness of cross-sabbaticals.

(c) Create a variety of tangible and sufficiently attractive incentives that will motivate private sector institutions to fund both accounting faculty and faculty research, to provide practice materials for academic research and for participation of professionals in behavioral and field study projects, and to encourage practicing accountants to pursue careers as academically and professionally qualified faculty.

**Recommendation 4.** Develop and maintain consistent demographic and higher education program profile data.

**Recommendation 5.** Encourage the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association jointly to form a commission to provide a timely study of the possible future structure of higher education for the accounting profession.

#### **Firm Structure and Finances Recommendations**

✓ **Recommendation 1.** Urge the Securities and Exchange Commission (SEC), and Congress as appropriate, to provide for the creation by the Public Company Accounting Oversight Board (PCAOB) of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.

**Recommendation 2.** Encourage greater regulatory cooperation and oversight of the public company auditing profession to improve the quality of the audit process and enhance confidence in the auditing profession and financial reporting.

(a) Institute the following mechanism to encourage the states to substantially adopt the mobility provisions of the Uniform Accountancy Act, Fifth Edition (UAA): If states have failed to adopt the mobility provisions of the UAA by December 31,

2010, Congress should pass a federal provision requiring those states to adopt these provisions.

✓ **(b) Require regular and formal roundtable meetings of regulators and other governmental enforcement bodies in a cooperative effort to improve regulatory effectiveness and reduce the incidence of duplicative and potentially inconsistent enforcement regimes.**

(c) Urge the states to create greater financial and operational independence of their state boards of accountancy.

✓ **Recommendation 3.** Urge the PCAOB and the SEC, in consultation with other federal and state regulators, auditing firms, investors, other financial statement users, and public companies, to analyze, explore, and enable, as appropriate, the possibility and feasibility of firms appointing independent members with full voting power to firm boards and/or advisory boards with meaningful governance responsibilities to improve governance and transparency of auditing firms.

✓ **Recommendation 4.** Urge the SEC to amend Form 8-K disclosure requirements to characterize appropriately and report every public company auditor change and to require auditing firms to notify the PCAOB of any premature engagement partner changes on public company audit clients.

✓ **Recommendation 5.** Urge the PCAOB to undertake a standard-setting initiative to consider improvements to the auditor's standard reporting model. Further, urge that the PCAOB and the SEC clarify in the auditor's report the auditor's role in detecting fraud under current auditing standards and further that the PCAOB periodically review and update these standards.

**Recommendation 6.** Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report.

**Recommendation 7.** Urge the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating (a) information required by the EU's Eighth Directive, Article 40 Transparency Report deemed appropriate by the PCAOB, and (b) such key indicators of audit quality and effectiveness as determined by the PCAOB in accordance with Recommendation 3 in Chapter VIII [Concentration and Competition] of this Report. Further, urge the PCAOB to require that, beginning in 2011, the larger auditing firms file with the PCAOB on a confidential basis audited financial statements.

#### **Concentration and Competition Recommendations**



✓ **Recommendation 1.** Reduce barriers to the growth of smaller auditing firms consistent with an overall policy goal of promoting audit quality. Because smaller auditing firms are likely to become significant competitors in the market for larger company audits only in the long term, the Committee recognizes that Recommendation 2 will be a higher priority in the near term.

✓ (a) Require disclosure by public companies in their registration statements, annual reports, and proxy statements of any provisions in agreements with third parties that limit auditor choice.

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✓ **Recommendation 2.** Monitor potential sources of catastrophic risk faced by public company auditing firms and create a mechanism for the preservation and rehabilitation of troubled larger public company auditing firms.

✓ (a) As part of its current oversight over registered auditing firms, the PCAOB should monitor potential sources of catastrophic risk which would threaten audit quality.

✓ (b) Establish a mechanism to assist in the preservation and rehabilitation of a troubled larger auditing firm. A first step would encourage larger auditing firms to adopt voluntarily a contingent streamlined internal governance mechanism that could be triggered in the event of threatening circumstances. If the governance mechanism failed to stabilize the firm, a second step would permit the SEC to appoint a court-approved trustee to seek to preserve and rehabilitate the firm by addressing the threatening situation, including through a reorganization, or if such a step were unsuccessful, to pursue an orderly transition.

**Recommendation 3.** Recommend the PCAOB, in consultation with auditors, investors, public companies, audit committees, boards of directors, academics, and others, determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators. Assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.

✓ **Recommendation 4.** Promote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits.



✓ (a) Compile the SEC and PCAOB independence requirements into a single document and make this document website accessible. The AICPA and state boards of accountancy should clarify and prominently note that differences exist between the SEC and PCAOB standards (applicable to public companies) and the AICPA and state standards (applicable in all circumstances, but subject to SEC and PCAOB standards, in the case of public companies) and indicate, at each place in their standards where differences exist, that stricter SEC and PCAOB independence requirements applicable to public company auditors may supersede or supplement the stated requirements. This compilation should not require rulemaking by either the SEC or the PCAOB because it only calls for assembly and compilation of existing rules.

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**Recommendation 6.** Enhance regulatory collaboration and coordination between the PCAOB and its foreign counterparts, consistent with the PCAOB mission of promoting quality audits of public companies in the United States.

**6**

**Department of the  
Treasury**

Investor Advisory Group  
Public Company Accounting Oversight Board  
Working Group on U.S. Treasury Advisory  
Committee on the Auditing Profession

August 15, 2016

The Honorable  
Jacob J. Lew  
Secretary of the Treasury  
Department of the Treasury  
1500 Pennsylvania Avenue, NW  
Washington, D.C. 20220

Dear Mr. Secretary:

In 2007 the U.S. Secretary of the Treasury, the Honorable Henry M. Paulson, Jr., announced and appointed an Advisory Committee on the Auditing Profession (ACAP) "...to consider and develop recommendations relating to the sustainability of the auditing profession." Secretary Paulson appointed twenty one members to the Committee. The members of the committee had a variety of backgrounds including business executives and corporate board members, former Securities and Exchange Commission (SEC) and Federal Reserve Chairmen, former SEC chief accountants, auditors, investors and attorneys. A year later in October 2008, the ACAP issued its recommendations.

On its website, the Treasury Department states:

The Committee considered, among other things, the auditing profession's ability to cultivate, attract, and retain the human capital necessary to meet developments in the business and financial reporting environment and ensure audit quality for investors; audit market competition and concentration and the impact of the independence and other professional standards on this market and investor confidence; and the organizational structure, financial resources, and communication of the auditing profession.<sup>1</sup>

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<sup>1</sup> See <https://www.treasury.gov/about/organizational-structure/offices/Pages/acap-index.aspx>

As set forth at <https://www.treasury.gov/press-center/press-releases/Pages/hp1158.aspx>, the ACAP made approximately 18 recommendations submitted to the Secretary of the Treasury. These recommendations focused on the auditing profession which has an important role in maintaining the credibility and reliability of the U.S. capital markets. The recommendations in the final report of the ACAP were directed to the Securities and Exchange Commission (SEC), the Public Company Accounting Oversight Board (PCAOB), the National Association of State Boards of Accountancy (NASBA), the American Institute of Certified Public Accountants (AICPA) and the American Accounting Association (AAA). These recommendations focused on:

1. Improving accounting education and strengthening human capital;
2. Enhancing auditing firm governance, transparency, responsibility, communications, and audit quality; and
3. Ways to increase audit market competition and auditor choice.

The PCAOB Investor Advisory Group (IAG) has been asked to make a presentation to the PCAOB on October 27, 2016 regarding the steps that have been taken to implement the recommendations made by the ACAP. The IAG, comprised of investor representatives and advocates, meets annually with the PCAOB board members and staff to discuss issues important to investors, the PCAOB and auditing profession<sup>2</sup>. At the October 2016 meeting, a working group of the IAG will be making a presentation to the members of the PCAOB with respect to the progress that has been made in the intervening eight years since the issuance of the ACAP final report. Accordingly, the working group is diligently undertaking to identify the actions taken to date, by each entity to which the recommendations were addressed, as well as what obstacles, if any, they have faced in addressing the ACAP recommendations.

To that end, the working group would appreciate it, if the U.S. Treasury Department staff could provide a response to the working group, with respect to what steps the Department has taken to monitor the progress made in implementing the ACAP recommendations. Such a response would be helpful in ensuring our report to the PCAOB is as comprehensive as possible. In order to adequately consider the response, it would be appreciated if it could be received by no later than September 15, 2016.

You can address your response to the working group co-chair. Parveen Gupta, Lehigh University, 621 Taylor Street, College of Business and Economics, Lehigh University, Bethlehem PA, 18015. Please do not hesitate to Call Mr. Gupta (610-758-3443) or Mr. Turner (303-956-4895) if you have any questions.

This project is being undertaken by the IAG working group and its members. As such, it is not a project being undertaken by the PCAOB or its staff. However, we hope it will result in

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<sup>2</sup> Two of the members of the PCAOB IAG were members of the ACAP. Other members of the IAG participated in the deliberations of the ACAP by testifying before it and providing comments.

a report that is informative and helpful to the PCAOB in its endeavors. Your assistance in that regards will be greatly appreciated.

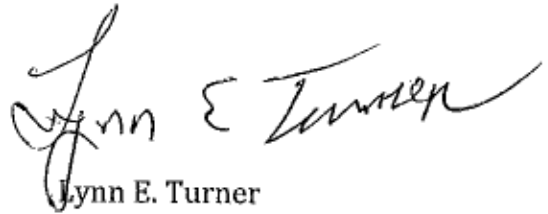
Again, we greatly appreciate your support.

Sincerely,



Parveen Gupta

Investor Advisory Group  
Working Committee Co-Chair



Lynn E. Turner  
Investor Advisory Group  
Working Committee Co-Chair