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Report from the Working Group on the ACAP Recommendations

Parveen Gupta (Co-Lead)

Lynn Turner (Co-Lead)

Mary Bersot

Grant Callery

Joe Carcello

Norman Harrison

Bess Joffe

Damon Silvers

ACAP Recommendations

Our Charge

- Report on the Progress towards implementation of the U.S. Department of Treasury's Advisory Committee on the Auditing Profession Recommendations (“ACAP Recommendations”)
- Highlight the importance of those recommendations to investors
- Prioritize the ACAP Recommendations that have not yet been successfully implemented

ACAP Recommendations

ACAP Overview

- Advisory committee to U.S. Treasury Department
 - Study the sustainability of the auditing profession
 - 21 members
 - Significant deliberations, Public hearings, exposure drafts
- Final recommendations eight years ago – October, 2008
- Recommendations in three major areas
 - Concentration and competition
 - Firm structure and finances
 - Human capital




ACAP Recommendations

ACAP Recommendations Promote Investor Protection and Capital Formation

- ❑ Provide investors with greater transparency on the quality of public company audits
- ❑ Measure and disclose information to investors regarding actual audit quality
- ❑ Clearer communication of audit results and financial statement risks
- ❑ Establish accountability for who leads the audit
- ❑ Create a national research center to improve fraud detection and prevention
- ❑ Improve transparency and governance of audit firms of public companies
- ❑ Increase the competency of those who perform public company audits




ACAP Recommendations

Progress on Implementing ACAP Recommendations

- ❑ Progress report based on responses provided to the working group by AAA, AICPA, NASBA, PCAOB and the SEC.
- ❑ For details see the report and Appendix 1 for copies of the letters received from various organizations
- ❑ Color coded scheme
 -  = Recommendation has been acted upon with successful results
 -  = Some implementation has occurred but more remains to be done
 -  = Little or no meaningful progress has occurred






ACAP Recommendations

Progress on Human Capital Recommendations (1)

Recommendations	Sub-Recommendations	Organizations	Status
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.	AAA, AICPA, NASBA	
	(b) Reflect real world changes in the business environment more rapidly in teaching materials.	AAA, AICPA, NASBA	
	(c) Require that schools build into accounting curricula current market developments.	AAA, AICPA, NASBA	




ACAP Recommendations

Progress on Human Capital Recommendations (2)

Recommendations	Sub-Recommendations	Organizations	Status
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.	AAA, AICPA	
	(b) Institute initiatives to increase the retention of minorities in the profession.	AAA, AICPA	
	(c) Emphasize the role of community colleges in the recruitment of minorities into the auditing profession.	AAA, AICPA	
	(d) Emphasize the utility and effectiveness of cross-sabbaticals and internships with faculty and students at Historically Black Colleges and Universities.	AAA, AICPA	
	(e) Increase the numbers of minority accounting doctorates through focused efforts.	AAA, AICPA	



ACAP Recommendations

Progress on Human Capital Recommendations (3)

Recommendations	Sub-Recommendations	Organizations	Status
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.	AAA, AICPA	
	(b) Emphasize the utility and effectiveness of cross-sabbaticals.	AAA, AICPA	
	(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.	AAA, AICPA	



ACAP Recommendations

Progress on Human Capital Recommendations (4-5)

Recommendations	Sub-Recommendations	Organizations	Status
Recommendation 4. Develop and maintain consistent demographic and higher education program profile data.		AAA	
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.		AAA, AICPA	



ACAP Recommendations

Progress on Concentration and Competition Recommendations (1)

Recommendations	Sub-Recommendations	Organizations	Status
<p>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.</p>	<p>(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.</p>	<p>SEC</p>	
	<p>(b) Include representatives of smaller auditing firms in committees, public forums, fellowships, and other engagements.</p>	<p>AICPA, PCAOB, SEC</p>	


ACAP Recommendations

Progress on Concentration and Competition Recommendations (2)

Recommendations	Sub-Recommendations	Organizations	Status
<p>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.</p>	<p>(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.</p>	<p>PCAOB, SEC</p>	
	<p>(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.</p>	<p>PCAOB, SEC</p>	



ACAP Recommendations

Progress on Concentration and Competition Recommendations (3)

Recommendations	Sub-Recommendations	Organizations	Status
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.		AAA, PCAOB	



ACAP Recommendations

Progress on Concentration and Competition Recommendations (4)

Recommendations	Sub-Recommendations	Organizations	Status
<p>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.</p>	<p>(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.</p>	<p>AICPA, NASBA, PCAOB, SEC</p>	
	<p>(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.</p>	<p>AICPA, NASBA, PCAOB</p>	


ACAP Recommendations

Progress on Concentration and Competition Recommendations (5-6)

Recommendations	Sub-Recommendations	Organizations	Status
Recommendation 5. Adopt annual shareholder ratification of public company auditors by all public companies.		SEC	
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.		PCAOB	




ACAP Recommendations

Progress on Firm Structure and Finances Recommendations (1)

Recommendations	Sub-Recommendations	Organizations	Status
<p>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.</p>		PCAOB, SEC	




ACAP Recommendations

Progress on Firm Structure and Finances Recommendations (2)

Recommendations	Sub-Recommendations	Organizations	Status
<p>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.</p>	<p>(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.</p>	<p>NASBA</p>	
	<p>(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>	<p>NASBA, PCAOB, SEC</p>	
	<p>(c) Urge the states to create greater financial and operational independence of their state boards of accountancy.</p>	<p>NASBA</p>	



ACAP Recommendations

Progress on Firm Structure and Finances Recommendations (3-5)

Recommendations	Sub-Recommendations	Organizations	Status
<p>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.</p>		<p>NASBA, PCAOB, SEC</p>	
<p>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.</p>		<p>PCAOB, SEC</p>	
<p>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.</p>		<p>PCAOB, SEC</p>	

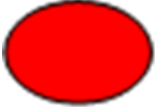
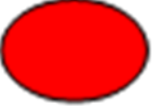

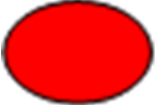

ACAP Recommendations

Progress on Firm Structure and Finances Recommendations (6-7)

Recommendations	Sub-Recommendations	Organizations	Status
<p>Recommendation 6. Urge the PCAOB to undertake a standard-setting initiative to consider mandating the engagement partner's signature on the auditor's report.</p>		PCAOB	
<p>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.</p>		PCAOB	

ACAP Recommendations

Working group's Five priority recommendations for action in near term

- ❑ Audit quality indicators (C&C #3) 
- ❑ Creation of national fraud center (F&F #1) 
- ❑ Improving the audit report (F&F #5) 
- ❑ Enhancing firm transparency and governance (F&F #7) 
- ❑ Human capital – upgrading accounting and business curriculum (HC #1) 

ACAP Recommendations

Audit quality indicators (C&C #3)

- Investors vote on approval of auditors for many, but not all public companies
 - Today investors do not have information to make informed decisions
 - PCAOB inspection reports and other data raise significant concerns re quality
 - It is a concern that the profession is not able to adequately measure , manage and make transparent audit quality indicators
- A key indicator can be the early rotation of an audit partner
 - Information should be disclosed to investors so they are informed
- PCAOB should make inspection reports transparent to provide useful information to investors

ACAP Recommendations

Creation of national fraud center (F&F #1)

- PCAOB outlined plans for a fraud center in 2010
 - Advertised for position, but never moved forward
 - Created CEA and ORA
 - However, these lack the focus of a national fraud center
- National fraud center
 - Focus on research and innovation of fraud detection and prevention
 - Should be led by full – not part time – staff
 - Full exchange of information and cooperation with other PCAOB units
 - Develop database and grant appropriate public access

ACAP Recommendations

Improving the audit report (F&F #5)

- Audit report is primary means of auditor communicating to investor
- Audit Partner disclosure increases disclosure
 - Falls short of audit partner signature used in other countries
- Audit report should also
 - Clarify and state responsibility for detection of fraud
 - Report critical audit matters directly to investors
 - Disclose tenure of auditor, that auditor is independent
 - Enhance the investors understanding of the audit, audit results, financial statement risks

ACAP Recommendations

Enhancing firm transparency and governance (F&F #7)

- ❑ U.S. Auditor has a legislated, important role in the capital markets and obligation to investors and the public
- ❑ To avoid a too big to fail situation, audit firms should be held to similar standards of transparency and governance for public companies
 - Without adequate transparency and governance, risk of too big to fail increases
- ❑ Little progress to date beckons action
 - Review of U.S. transparency reports finds they fall short of European disclosures
 - Lack of financial information regarding sustainability
 - U.S. Governance structures are internal board of partners, lack independence and oversight

ACAP Recommendations

Human capital – upgrading curriculum (HC #1)

- ❑ Auditing is a human capital intensive activity
- ❑ Focus on the quality of the human capital supply chain, not only on the quantity
- ❑ Hurdles in the way
 - Financial return in auditing
 - University higher administration doesn't understand the “public interest’ role of accounting programs in business schools
 - Faculty Publish or perish
 - Checklist implementation of the 150-credit hour requirement
 - Universities focus on revenue-1 year MS in accounting programs
 - Lack of uniformity in state board requirements to sit for the CPA exam
 - Accrediting agencies not pushing for public interest mission of accredited accounting programs
 - Rise in the faculty ranks without practical experience and CPA qualification

ACAP Recommendations

Human capital – upgrading curriculum (HC #1)

- Potential actions to consider to move the needle on forcing business schools/accounting programs to ensure relevancy and currency of their curriculum
 - NASBA/AAA to work closely with the PCAOB to understand inspection findings to determine the extent to which lack of sufficient training and/or professional judgment was at the root cause of deficient audits. This information should drive NASBA/AAA to work with individual state boards to adjust CPA license requirements in real time
 - NASBA/AAA to create a task force to consider implementing the 150-credit hour requirement through post-graduate education in accounting
 - Accrediting agencies to reconsider their focus from “mission-driven” approach to “public interest” mission
 - PCAOB awarding scholarships from the fines only to students pursuing post graduate education in accounting

ACAP Recommendations

Questions

