

September 2, 2015

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W. Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 041.

Deloitte & Touche LLP (“D&T”) is pleased to respond to the request for comments from the Public Company Accounting Oversight Board (the “PCAOB” or the “Board”) on its *Concept Release on Audit Quality Indicators and Notice of Roundtable* (“the concept release”), PCAOB Release No. 2015-005, and PCAOB Rulemaking Docket Matter No. 041 (July 1, 2015).

EXECUTIVE SUMMARY

We fully support the exploration and development of audit quality indicators (AQIs), and commend the PCAOB on its robust and thoughtful concept release. We applaud the transparent approach the PCAOB has used in the development of the concept release; discussion of AQIs at several PCAOB Standing Advisory Group meetings has provided meaningful opportunities for input from various stakeholders, helped to educate many on the reasons for pursuing the use of AQIs and the ultimate goals of the PCAOB, and resulted in elevating the dialogue across the profession and within accounting firms about how AQIs may be used. We remain committed to continuing to collaborate with the PCAOB on this important initiative and welcome the opportunity to provide feedback and engage in future dialogue as the PCAOB considers input from the concept release and plans its related fall roundtable.

Based on our experiences to date through the Center for Audit Quality (CAQ) project pilot testing and internal study (as discussed further herein), we believe AQIs have the potential to be a useful tool in enhancing audit firms’ management and monitoring of audit quality. We are in the early stages of utilizing AQIs internally as a monitoring tool. We believe, as more experience is gained and the AQIs are further tested and proven, they will become an effective monitoring tool for audit firms in assessing audit quality.

We also believe that certain AQIs could help audit committees understand more about the audit process, the firm engaged to conduct the audit, and considerations for assessing audit quality. As audit committees have the responsibility for the appointment, compensation, and oversight of the external auditor, discussing relevant and meaningful AQIs with audit committees may help to provide additional insights and information to the audit committee to enhance their ability to meet their responsibilities.

In practice, we have found that to be most useful and relevant it is critical to allow for flexibility in the determination and calculation of AQIs for various uses and constituents. Accordingly, we do not believe that a specific list of required individual AQIs or a certain AQI program should be mandated at this time. Rather, in order to provide an opportunity for innovation in the use of AQIs and to allow time for audit committees and auditors to learn about the best way to utilize AQIs, we believe that, at least for the time

being, the internal monitoring and external reporting of AQIs to audit committees should remain voluntary. Such voluntary communications, paired with further collaboration among audit firms and the PCAOB, will allow for additional experience to be gained and lessons learned prior to the PCAOB considering any potential next steps with respect to specific rule-making. We provide additional observations and more detailed discussion on these matters stated above in the remainder of this letter, and look forward to a collaborative effort continuing to explore the development of AQIs.

OUR EXPERIENCE WITH AQIs AND POTENTIAL APPROACHES

Regarding external communication of AQIs, our experiences outlined below result in our view that AQIs should be reported on a voluntary basis to audit committees for the time being, in order to continue the learning process, refine metrics, and enable further assessment of the context required for audit committees to understand and assess the usefulness of AQIs.

Pilot Testing Through the Center for Audit Quality AQI Project

Our efforts and active participation in the CAQ AQI pilot testing included discussing with a limited number of audit committees a set of approximately twelve¹ quantitative metrics focused on the following themes: engagement team knowledge, experience, workload, monitoring (including internal and external inspection results), and auditor reporting (including restatement statistics). The pilot testing also included qualitative discussions regarding firm leadership, tone at the top, training, and monitoring, among other matters. The discussions with audit committees took part over the course of a year and mostly occurred during two phases of the audit (at the beginning of the audit and at the end of the audit). We found that our own perspectives, those of the collective profession, and also the views of audit committee members became more fine-tuned as the project progressed through the pilot testing phases.

We also found that each audit committee had different perspectives, needs, and requests with respect to AQIs. As a result, the focus of the discussions varied by audit committee, depending upon which AQIs they found most useful and what supplemental metrics and information they required for additional information and context. Each discussion was tailored to each audit committee’s unique needs and interests, helping them achieve and meet their oversight responsibilities in a manner they believed most valuable. Communicating and customizing AQIs for each audit committee fostered an in-depth dialogue between the auditor and audit committee, enhanced audit committee discussions about audit quality, and allowed for tailoring of specific information to address the needs of a variety of audit committees and sets of circumstances.

In tailoring AQIs to improve relevance to each audit committee, it became apparent that developing systematic reporting of AQIs would be very complex. In addition, given that the needs of each audit committee varied, more study is required to avoid developing an automated approach that could inhibit further enhancement of the AQIs and limit the ability to tailor the information, thereby causing the risk of limiting overall usefulness and relevancy of the AQIs.

Further, as we listened to and debated perspectives, both internal and external, our approach continued to be more refined and over time ultimately provided a more useful discussion to each audit committee who

¹ In some cases all twelve were not included in the pilot testing, in others additional metrics were added based on audit committee request.

participated in the pilot program. These views continue to evolve as we have the opportunity to discuss and refine the AQIs further to meet the needs of various audit committees.

Internal Office-Level AQIs

In addition to the CAQ pilot, we have worked internally to develop a set of office-level indicators for the purpose of enhancing our management and monitoring of audit quality for quarterly reporting to office, regional, and national leadership. The indicators we are tracking on an office basis are focused on the following themes: hours and headcount composition, utilization, timing of audit hours, engagement of specialists, consultations with others outside the audit engagement team, audit quality milestones throughout the audit cycle, and mandatory learning. Certain office-level indicators overlap with the approximately 12 quantitative metrics subject to CAQ pilot testing for communication to audit committees and with certain of those presented in the PCAOB's concept release; however, others are potentially only relevant to enhancing our firm's management and monitoring of audit quality.

We are still in the early stages of utilizing AQIs for internal management and monitoring purposes. Through collaboration with leadership and various groups within our system of quality control, our internal AQIs are continually being challenged and refined to balance the ability to report on consistent and meaningful AQIs while minimizing the risk of false positive and negatives. We believe this philosophy of continuous improvement will result in more useful and robust office-level information. Thus far, we have found the office-level indicators, when discussed with other factors that could affect audit quality, have aided in highlighting offices where outliers have been identified and are in need of additional leadership attention. However, we believe more time and study is needed to determine if these office level indicators are helping to successfully consider root causes and drive appropriate action.

Our experience, again, with our internal development of office-level AQIs has led us to believe the process of developing and presenting comparative audit quality indicators is complex and requires experimentation in order to make them the most relevant and useful to the audience, in this case leadership. Furthermore, developing and continuously improving this set of indicators requires collaboration among multiple groups within our own firm, and the usefulness of these indicators is still being assessed.

Considerations for Voluntary Approach

Maintaining a voluntary AQI program and allowing audit firms to continue to experiment with communicating metrics to audit committees would allow firms and audit committees to identify and focus on which AQIs are most relevant, useful, and meaningful to audit quality. If voluntary, engagement teams may prioritize the most relevant and useful information to meet the needs of their audit committees, thereby potentially limiting consistency and comparability among engagements and firms. In addition, the impact could be greater if audit committees are requesting the information from the auditors that they feel is most relevant, as opposed to the information being mandated with an additional regulatory requirement.

As previously stated, flexibility in the determination and calculation of AQIs is critical to meet the needs and uses of various audit committees. For example, one of the pilot engagement teams expanded the CAQ's proposed AQIs relating to demonstrating knowledge and experience of key engagement team members, to more effectively capture the engagement team's collective experience. The CAQ's proposed calculation for this AQI highlighted only the number of years on the engagement, in the industry, at the

firm and at the present level, whereas for this particular situation it was more meaningful to address industry experience through a more qualitative narrative and discussion, accompanied by a quantitative analysis of the engagement team composition by level as a percentage of the total engagement team.

Voluntary communications will also allow for additional experience to be gained and lessons learned to continuously improve the communication of AQIs. For example, an important lesson learned during the pilot testing was how to best integrate the discussion of AQIs with other communications required under PCAOB standards and effectively engage in dialogue incorporating all relevant concepts related to audit quality and the performance of the audit.

Considerations for Mandatory Approach

In contrast, if the PCAOB were to pursue a mandatory approach and require reporting to the audit committee or to the public, there are a number of risks and challenges that should be considered, including the following:

- *Documentation exercise:* Mandatory requirements have a likelihood of creating a checklist approach in communicating AQIs to the audit committee. This could dilute the importance of the narrative discussions surrounding the communication of AQIs and the result may be lack of interest and limited consideration by the audit committee of the AQI information. This concern has been raised by audit committee members in our discussions with them about the potential use of AQIs.
- *Lack of context:* In our experience, viewing any one AQI, or even many of them, without consideration and discussion of other factors affecting audit quality could be misleading. Without overall context, there could be unintended consequences related to misinterpreting the AQIs, thus affecting the perceived value and quality of the audit, as well as the usefulness of the AQIs. In our pilot testing efforts, audit committees often requested additional context and explanatory information in order to enhance their understanding of the metrics discussed. AQIs are one of many means for audit committees to engage in and oversee audit quality, so it is important to maintain appropriate context and consider this information in totality.
- *Challenge of balancing consistency with flexibility, relevance, and usefulness:* If AQIs are mandated across the profession, the calculation and precision of the AQIs should be clearly defined and capable of being consistently calculated. We encountered complexities reporting AQIs internally, so developing standard calculations across the profession could prove to be challenging. Further, if consistency is prioritized more heavily, it may prove counterproductive because it could be at the expense of relevance, usefulness, and the ability to tailor the information. This is a fundamentally difficult issue to address and consider, as demonstrated by the number of questions posed in the concept release concerning consistency. We believe at this stage, focusing on relevance and usefulness of AQIs should be the priority.
- *Potential costs:* While gathering information for a discrete number of meaningful and useful AQIs will involve costs and have some economic impact, the efforts and costs would be justified if AQIs are tailored to be the most relevant and useful in each set of circumstances and for each purpose. In our experience, AQIs can result in false positives, both at the engagement and office level, which can be distracting, costly, and negatively affect quality and audit committee focus.

Depending on the number and extent of AQIs developed and used, and the scope of reporting, the gathering and reporting of AQIs could become overly burdensome, impractical, and distracting from our firm's ability to effectively monitor and manage audit quality and execute quality audits.

- *A principles-based approach:* If the PCAOB were to move forward in contemplating the development of a mandatory requirement, it could be focused on requiring the auditor and audit committee to come to agreement on (1) the AQI-related information the audit committee would like to have in order to assess the risks and identify actions that should be taken to assess the inputs related to the quality of the audit, and (2) which metrics would be most useful to them in assessing the quality at the end of the engagement. The potential requirement could provide examples of what AQIs might be considered, but the requirement would be for the auditor and audit committee to come to a documented understanding of what will be provided and then for the auditor to provide and discuss the AQI information based on that documented agreement.

SUMMARY AND NEXT STEPS

As a result of the above, we support a period of voluntary application and after a period of further study, a thoughtful reassessment of (1) the audience to whom AQIs should be communicated, (2) which AQI's are most relevant and useful to communicate, and (3) whether the communication should be mandatory. Although some of the topics included within the PCAOB's list of 28 potential indicators are already discussed with audit committees as part of an auditor's regular communications with the audit committee,² we are in the very early stages of developing metrics and understanding how the metrics relate directly to audit quality and, as stated previously, we believe more can be learned through further voluntary communications and pilot-testing.

Based on our above observations, we believe potential next steps for the PCAOB could include the following:

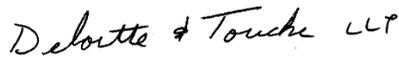
- Encourage experimentation of the use of AQIs by audit firms to enhance management and monitoring of audit quality, and in discussions with audit committees. The PCAOB may also consider whether a formal pilot testing program with audit firms and audit committees could be undertaken.
- Consider the results of such experimentation by obtaining direct feedback from audit firms, audit committees, and others as appropriate.
- Consider making this a centerpiece of the PCAOB's audit committee engagement agenda, to elevate interest and promote audit committees asking for this information.
- Continue to engage in active and transparent dialogue regarding the feedback received and potential direction of the PCAOB's project based on that feedback.

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² For example, auditors and audit committees discuss matters related to the overall audit strategy and timing, significant risk areas, audit fees, audit effort, independence, PCAOB inspection results and modifications to the auditor's opinion. In addition, audit committees are typically aware of information regarding expertise and experience of audit personnel, involvement of specialists and technical experts, and staffing of the audit.

D&T appreciates the opportunity to provide our perspectives on these important topics. Our comments are intended to assist the PCAOB in analyzing the relevant issues and potential effects of developing AQIs. We appreciate the opportunity to provide feedback on this important initiative and commend the PCAOB on its achievements thus far. We would be pleased to engage in further dialogue on these topics and participate in further experimentation or pilot testing of AQIs under the leadership of the PCAOB. If you have any questions or would like to discuss these issues further, please contact Thomas Omberg at 212-436-4126, Alex Schillaci at 203-761-3489, or Dave Sullivan at 714-436-7788.

Very truly yours,

A handwritten signature in black ink that reads "Deloitte & Touche LLP". The signature is written in a cursive, flowing style.

Deloitte & Touche LLP

cc: James R. Doty, PCAOB Chairman
Lewis H. Ferguson, PCAOB Member
Jeanette M. Franzel, PCAOB Member
Jay D. Hanson, PCAOB Member
Steven B. Harris, PCAOB Member
Martin F. Baumann, PCAOB Chief Auditor and Director of Professional Standards

Mary Jo White, SEC Chair
Luis A. Aguilar, SEC Commissioner
Daniel M. Gallagher, SEC Commissioner
Michael S. Piwowar, SEC Commissioner
Kara M. Stein, SEC Commissioner
James V. Schnurr, SEC Chief Accountant
Brian T. Croteau, SEC Deputy Chief Accountant