PCAOB
PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

SPOTLIGHT

Staff Update on 2024 Inspection Activities

March 2025

CONTENTS

OVERVIEW

Under its founding statute, the Sarbanes-Oxley Act, the PCAOB was given a responsibility to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports. For more than 20 years, the Board and the PCAOB staff have worked tirelessly to fulfill this critical responsibility. One of the most important ways the PCAOB does so is through its inspection program.

PCAOB inspections are designed to assess an audit firm's compliance with applicable laws, rules, and standards, as mandated by the Sarbanes-Oxley Act. In 2024, the PCAOB advanced its mission by inspecting 171 PCAOB-registered public accounting firms ("audit firms" or "firms") and reviewing portions of over 800 public company (or "issuer" – see definition below under Terms Used in This Spotlight) audits.

This Spotlight focuses exclusively on the Division of Registration and Inspections' ("staff" or "we") results and activities from public company audit inspections conducted in 2024, as of its publication date. Results from the PCAOB's 2024 brokers and dealers ("broker-dealers") inspections will be issued by the Board later in 2025 in the "Annual Report on the Interim Inspection Program Related to Audits of Brokers and Dealers." To learn more, visit the Information for Auditors of Broker-Dealers section of the PCAOB's website.

Earlier Access to Inspection Reports

The Board has made it a priority to speed up the release of inspection results, ensuring that critical information gets into the hands of investors, audit committees, audit firms, and other market participants as soon as possible.

- In 2024, we published the 2023 inspection reports for annually inspected firms (including both the U.S. Global Network Firms and annually inspected U.S. Non-Affiliated Firms) in August, six months earlier than in the prior year, and nearly all the reports for triennially inspected firms were published within six months of the completion of those inspections.
- In 2025, we built on that progress, releasing the 2024 inspection reports for the U.S. Global Network Firms in March, another five months earlier.
- For triennially inspected firms, we are now publishing the reports, on average, within five months of the completion of those inspections.

We Observed Noticeable Improvements in 2024

PCAOB inspection results are an important marker for audit quality, and this Spotlight discusses how in 2024, we observed a tangible decrease in Part I.A[1] deficiency rates, on average, across all inspected firms. We also observed a substantial improvement, in the aggregate, among the largest firms we annually inspect. This improvement follows concentrated efforts by the PCAOB to encourage firms to reverse the trend of rising deficiency rates coming out of the pandemic

[1] For purposes of this Spotlight, Part I.A deficiency rates include engagements that we have inspected that have or are expected to have one or more comment forms that may lead to inspection findings included in Part I.A of an inspection report. For additional information, please refer to Terms Used in This Spotlight and the Appendix: About Part I.A Findings below.

and improve audit quality for investors. For 2024, key highlights include:

- **Overall Part I.A deficiency rates:** For all inspected firms, the aggregate Part I.A deficiency rate decreased to 39% in 2024, down from 46% in 2023.[2]
- **Big Four U.S. firms:** The aggregate Part I.A deficiency rate for the Big Four[3] U.S. firms – which as of December 31, 2024, collectively audit approximately 80% of the market capitalization of public companies listed on exchanges – decreased to 20% in 2024, from 26% in 2023.
- **U.S. Global Network Firms (GNF):** The aggregate Part I.A deficiency rate for the six[4] U.S. GNF firms decreased to 26% in 2024, from 34% in 2023.
- **U.S. Non-Affiliated Firms (NAF):** Results at the eight annually inspected NAF firms held steady, decreasing to 52% in the aggregate in 2024, compared to 53% in 2023.[5]
- **Triennial Firms:** Although the same firms are not inspected year-to-year, we saw improvements at the NAF and GNF triennially inspected firms. Aggregate deficiency rates at NAF triennially inspected firms decreased from 67% in 2023 to 61% in 2024, and GNF triennially inspected firms decreased from 35% in 2023 to 26% in 2024.[6]

We are encouraged by the decline in aggregate Part I.A deficiency rates observed in 2024, especially among the largest firms.

Drivers of Improvement

We have observed that firms have worked to improve the quality of their audits in various ways based on our inspections and on dialogue with firms during their remediation periods. Many of these actions were implemented in 2023 and reflected in the results of the inspections we performed in 2024. Example drivers of improvement by the larger firms include:

- **More in-person work.** Firms continued with policies requiring engagement teams to work on-site together for a portion of their work week.
- **More focused training.** Firms increased the training of less experienced staff.
- **More resources.** Firms strengthened national office resources dedicated to audit quality.
- **Better supervision and review.** Firms implemented programs or policies to increase supervision and review.

More Work To Do

While the progress made in 2024 is significant, overall deficiency rates are still high, and firms must continue to improve. We continue to encourage firms to review our Spotlights, which highlight common deficiencies, inspection observations, good practices, and reminders for auditors. These Spotlights provide important considerations and

[2] The overall Part I.A deficiency rates for 2024, as well as the results for the NAF Annual U.S. Firms and the Triennial Firms are estimates, as some inspection results have not been finalized, and the corresponding inspection reports have not yet been published at the time of this Spotlight's publication.

[3] The Big Four accounting firms are commonly known to be Deloitte & Touche LLP ("DT"), Ernst & Young LLP ("EY"), KPMG LLP ("KPMG"), and PricewaterhouseCoopers LLP ("PwC").

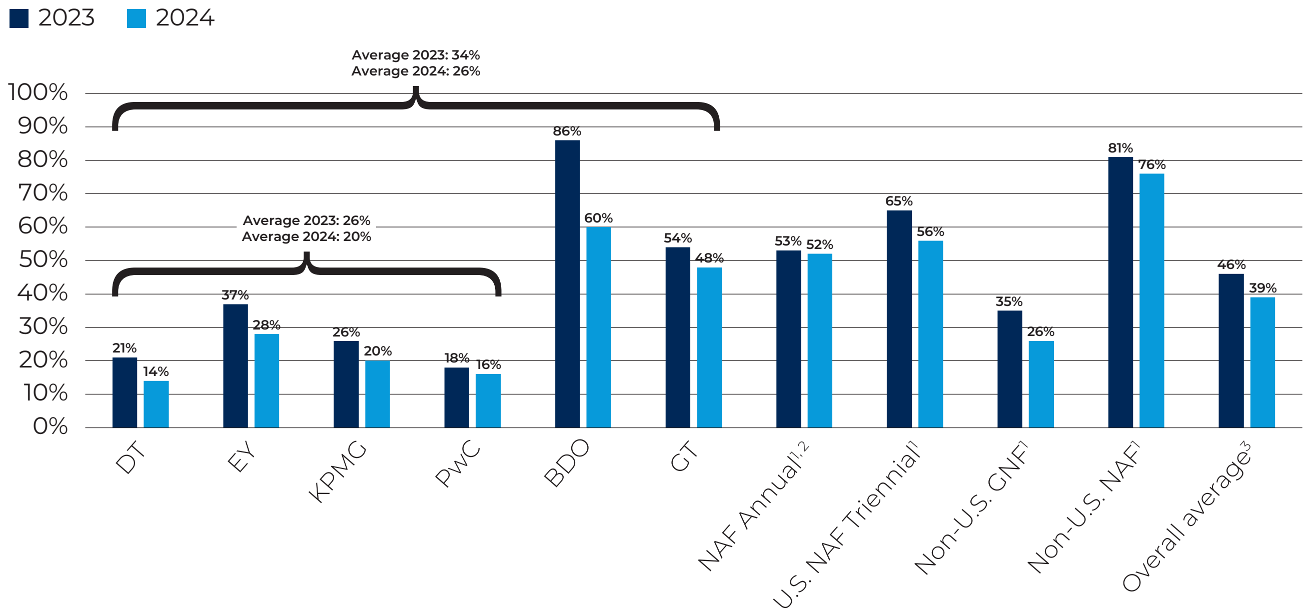
[4] The Big Four, BDO USA, P.C. ("BDO"), and Grant Thornton LLP ("GT").

[5] See Footnote 2.

[6] See Footnote 2.

examples to help firms improve audit quality. (See "PCAOB Efforts to Drive Improvement in Audit Quality" below.)

Figure 1 – Inspection Part I.A Deficiency Rates



[1] These 2024 results are estimates, because some inspection results have not been finalized, and the corresponding inspection reports have not yet been published. The triennial information for 2023 was an estimate in the "Staff Update on 2023 Inspection Activities" Spotlight and has been updated here to reflect published inspection reports.

[2] The 2023 results reflect data included in the public portion of the inspection reports of the eight registered non-affiliated U.S. firms that were inspected in 2023: Marcum LLP; RSM US LLP; Crowe LLP; WithumSmith+Brown, PC; Moss Adams LLP; Baker Tilly US, LLP; B F Borgers CPA PC; and Cohen & Company, Ltd. The 2024 results are estimates, as noted above, and also reflect the removal of one firm, B F Borgers CPA PC, as well as the addition of a new annually inspected firm, which will be disclosed when the inspection report for that firm is published. Additionally, in the narrative included in last year's Spotlight, the 2023 deficiency rate for NAF Annual U.S. firms was erroneously reported as 51% instead of 53%. This error occurred because the 51% figure reflected the deficiency rate for 2022.

[3] The 2024 overall result is an estimate, as indicated above.

PCAOB Efforts To Drive Improvement in Audit Quality

We have been working to reverse the decline in audit quality over several years through a variety of initiatives that have taken time to show the results that we are now observing. These initiatives include:

- **Publishing information to help firms improve.** Our Spotlights provide auditors with actionable recommendations and reminders that draw directly on insights from our inspection teams. Additionally, we highlight firm-wide quality control (QC) practices that may enhance a firm's QC system – and audit quality generally. We encourage auditors to consider how these insights may apply to both their specific audit engagements and broader QC systems, and to implement necessary changes proactively to enhance audit quality and ensure compliance with PCAOB standards.

- **Increasing transparency.** We are reporting on our inspection results, publishing inspection reports more quickly, and making findings data available on our website for both global network firms and non-affiliated firms.
- **Engaging regularly with firms.** In addition to day-to-day interactions, we have organized combined broker-dealer and small business forums to deepen our engagement with smaller firms. We are also encouraging feedback, especially from smaller firms, to ensure their unique perspectives are considered in the development of a proposed or amended standard or rule.
- **Focusing on smaller firms.** As part of our commitment to support smaller firms, we have launched a dedicated resource section on our website to provide targeted support. Additionally, we launched a new publication series, "Audit Focus," that is designed to provide easy-to-digest information to auditors, especially those auditing smaller public companies. These resources can be found on the Information for Smaller Firms page on the PCAOB website.
- **Assisting with implementation.** Staff working with the Chief Auditor are providing implementation resources for PCAOB standards and rules, such as the new QC standard.
- **Prioritizing remediation.** We are providing additional guidance concerning the remediation process and encouraging open and frequent two-way communication between audit firms and the PCAOB during the remediation process.
- **Engaging directly and regularly with U.S. audit committees.** Our engagement with audit committees has been a top priority, as we share a common goal of driving quality audits through effective oversight of external auditors.
- **Understanding the effect of culture on audit quality.** In December 2024, we published, "Insights on Culture and Audit Quality", which provided observations based on our QC inspection procedures and augmented interview procedures to research and understand the role that firm culture plays in the performance of high-quality audits.

Terms Used in This Spotlight

PCAOB Part I Inspection Report Sections

- **Part I.A** of our PCAOB inspection reports discusses deficiencies, if any, that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion(s) on the public company's financial statements and/or internal control over financial reporting (ICFR). For additional information, please refer to the Appendix: About Part I.A Findings below.
- **Part I.B** discusses certain deficiencies, if any, that relate to instances of noncompliance with PCAOB standards or rules other than those where the firm had not obtained sufficient appropriate audit evidence to support its opinion(s). This section does not discuss instances of potential noncompliance with SEC rules or instances of noncompliance with PCAOB rules related to maintaining independence.

- **Part I.C** discusses instances of potential noncompliance with U.S. Securities and Exchange Commission (SEC) rules or instances of non-compliance with PCAOB rules, if any, related to maintaining independence.

Other Terms

- **Audit firm categories** are defined in Section I below, along with a description of how we select firms for inspection.
- **Brokers and dealers** means entities that are registered with the SEC as a Broker (as defined in Section 3(a)(4) of the Securities Exchange Act of 1934 (Exchange Act)) or as a Dealer (as defined in Section 3(a)(5) of the Exchange Act), or that are registered with the SEC as both a broker and a dealer.
- **Comment form** is written communication with the audit firm when, after discussion with the audit firm, the inspection team still believes that a potential deficiency exists with the audit work. Firms are afforded an opportunity to respond to comment forms in writing, and the comment forms then are evaluated for inclusion in the firm's inspection report.
- **Engagement** refers to the firm's audit being reviewed.
- **Focus area** refers to the audit area(s) and/or procedure(s) of an audit selected for inspection, for which our inspection team will review the audit workpapers and interview engagement personnel.
- **GNF** stands for Global Network Firm and refers to our inspection program for firms that are members of a global network through which they affiliate with firms in other countries for various business and client service purposes.
- **Issuer** means an Issuer (as defined in Section 3 of the Exchange Act), the securities of which are registered under Section 12 of that Act, or that is required to file reports under Section 15(d) of that Act, or that files or has filed a registration statement that has not yet become effective under the Securities Act of 1933, and that it has not withdrawn. Please see PCAOB Rule 1001, Definitions of Terms Employed in Rules. In this Spotlight, the term "**public company**" is used to refer to an issuer.
- **NAF** stands for Non-Affiliated Firm and refers to our inspection program for firms that either do not affiliate with other firms (i.e., do not check box 5.2 on their annual Form 2) or are part of a network that is not one of the GNF Firms.
- **Workpapers** are the firm's documentation, typically in electronic form, documenting their audit procedures and conclusions for a particular engagement.

I. 2024 INSPECTIONS APPROACH

The PCAOB continued a rigorous program of inspections in 2024, primarily related to audits of public companies completed in 2024 for financial statements with a 2023 fiscal year-end. Each year, the PCAOB develops an inspection plan informed by, among other things, our inspection experience, current events that have an impact on audits, and other areas of concern. In 2024, our procedures anticipated financial reporting and audit risks driven by economic conditions, particularly those related to complex accounting or judgments required from the auditor and included an element of selection unpredictability.

Inspection Program Enhancements Implemented In 2024

Consistent with Goal 2 in the Board's Strategic Plan 2022-2026, we took steps to enhance our inspection program in 2024 using a data-driven and risk-based approach. Some of our enhancements include:

- Increasing the number of engagements selected for review at annually inspected firms in response to heightened risks in certain industry sectors.
- Conducting certain procedures on all engagements inspected to enhance the robustness, consistency, and comparability of inspections to assess audit firms' compliance with applicable laws, rules, and standards.
- Increasing our focus on a firm's culture of integrity and audit quality.
- Continuing to drive excellence across our inspection function by assessing the quality, consistency, and efficacy of our inspections.
- Improving the timeliness of inspection reports.

Frequency and Categorization of Firm Inspections

Generally, audit firms that audit public companies are selected for an inspection based on the number of public company audit reports they release each year. In accordance with the Sarbanes-Oxley Act, audit firms that issue audit reports for more than 100 issuers are inspected annually, and audit firms that issue audit reports for 100 or fewer issuers are inspected at least on a triennial basis.

We currently categorize audit firms in our inspection programs as follows:

- **U.S. GNF** – These firms are headquartered in the U.S. and are members of global networks through which they affiliate with firms in other countries for various business and client service purposes. Registered public accounting firms provide information about those affiliations in their annual reports on their annual Form 2. These U.S. firms all issue audit reports for more than 100 issuers each year and are therefore inspected annually.
- **Non-U.S. GNF** – These firms are headquartered outside of the U.S. and are members of global networks. Currently, these firms are generally inspected on a triennial basis because they issue audit reports for 100 or fewer issuers per year.
- **NAF Annual** – These firms are non-affiliated firms (as described above) that are inspected annually because they issue audit reports for more than 100 issuers per year. Currently, all NAF Annual firms are headquartered in the U.S.
- **U.S. NAF Triennial** – These firms are non-affiliated firms that are headquartered in the U.S. and are generally inspected on a triennial basis because they issue audit reports for 100 or fewer issuers per year.
- **Non-U.S. NAF** – These firms are non-affiliated firms that are headquartered outside of the U.S. and are generally inspected on a triennial basis because they issue audit reports for 100 or fewer issuers per year.

In Figure 2, the number of NAF Annual firms inspected can change year-to-year based on the number of issuer audit reports released by the firms.

Figure 2 – Number of Firms Inspected in Our Programs by Audit Firm Category

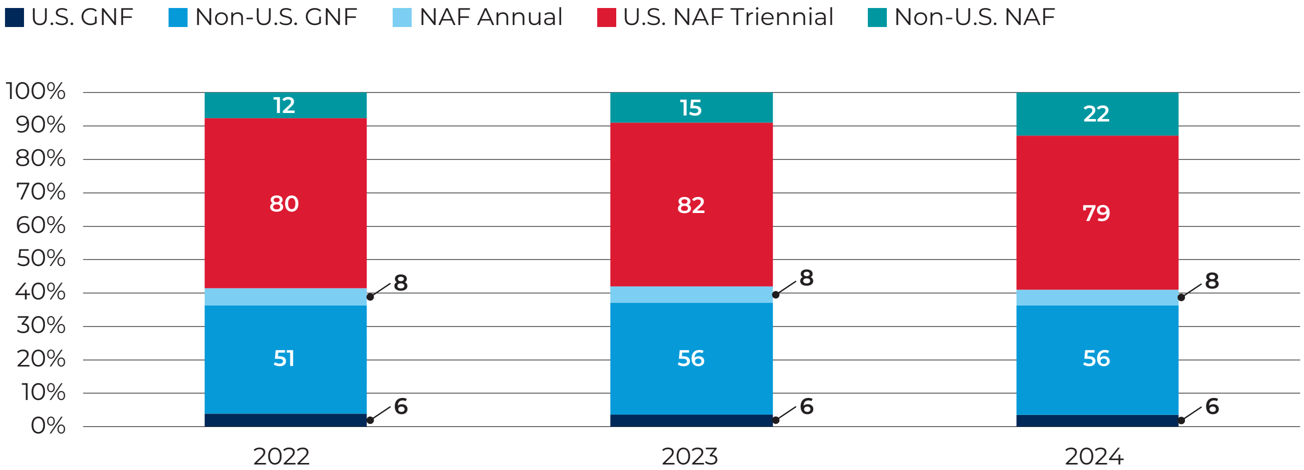
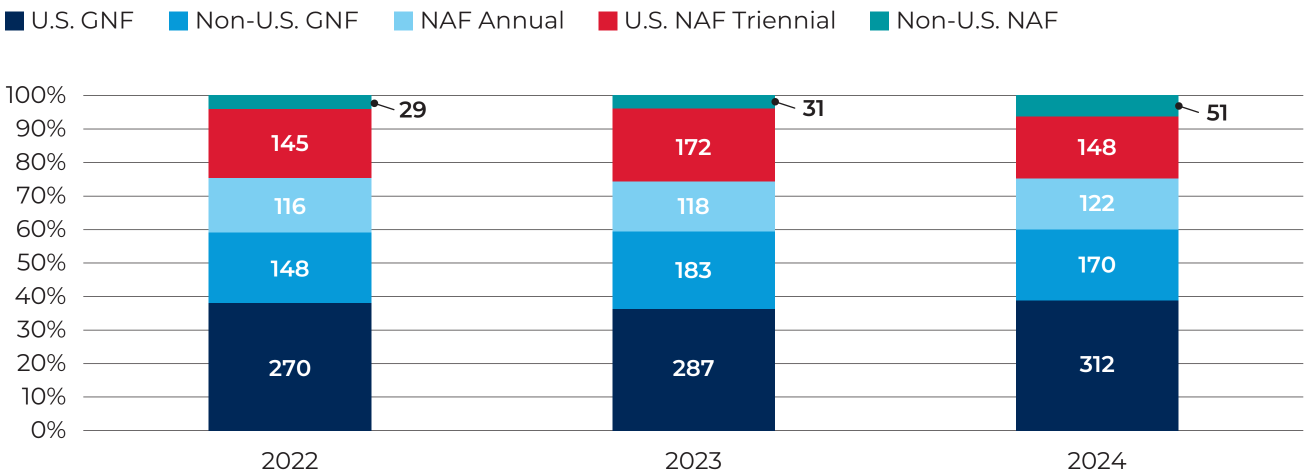


Figure 3 – Engagements Reviewed in Our Programs by Audit Firm Category



Key Inspection Considerations

The 2024 inspection plan (1) primarily covered the review of 2023 fiscal year-end audits with audit reports signed in early 2024 and (2) considered the business risks important for auditors to examine when planning and performing audit procedures. The considerations for our selection process were discussed fully in our Spotlight "Staff Priorities for 2024 Inspections."

A PCAOB inspection is not designed to review all aspects of a firm's quality control system, to review all of the firm's audits, or to identify every potential deficiency in the reviewed audits. We generally focus on audit areas we believe to be of greater complexity, areas of greater significance or with a heightened risk of material misstatement to the issuer's financial statements, and areas of recurring deficiencies. The inspected firm has no opportunity to limit or influence our selections.

How We Selected Engagements for Inspection

During 2024, our inspection procedures considered overall audit and business risks present for audits of public companies with a fiscal 2023 year-end. Various strategies were used to select individual audit engagements of public companies for review. Some were selected based on risk, and some were selected based on other strategies, including random selection, that enhance unpredictability. Our approach emphasized audits of:

- Regional banks and mutual funds with Level 3[7] investments, or other specific audit challenges.
- Public companies engaged in mergers and acquisitions activities or business combinations.
- Public companies in the information technology sector with complex revenue recognition.
- Public companies that require industry-specific or sector-specific accounting.
- Public companies that held significant assets that may have declined in value, such as collateralized commercial real estate debt.
- Public companies with material digital asset holdings or significant transactions related to digital assets.

For a full description of what the PCAOB inspects and how those inspections are conducted, please visit our website for information on PCAOB Inspection Procedures.

Target Team Focus in 2024

The PCAOB's target team is a group of inspectors who focus on emerging audit risks and issues. During 2024, target team inspection activities consisted of reviewing public company audits focused on the following topics:

- Initial audits by a successor auditor
- Risk assessments
- Auditor's assessments of a public company's use of artificial intelligence
- Biotech startups
- Audit firms' usage of shared service centers
- Cash flow statements, segment reporting, and earnings per share

Please look for our Spotlight publication reporting on these activities later in 2025.

Inspection Profile Information

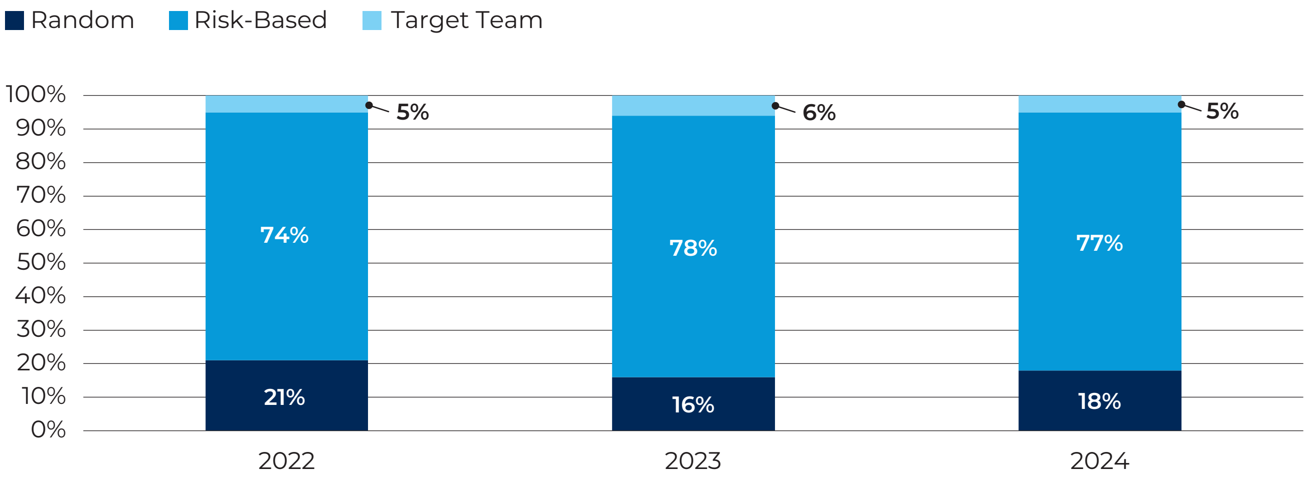
Figures 4 and 5 present profile information related to the audits inspected.

Annually inspected firms have a larger pool of engagements subject to our inspection, and we use a risk-based and random-based selection process to select which engagements we will review. We tailor the selection of engagements for review based on the size,

[7] Under generally accepted accounting principles in the U.S., there are three categories of inputs for use in determining an asset or liability's fair value. Those valued using Level 3 inputs are the most difficult to value because these inputs do not include readily available market information, and these assets are valued using unobservable inputs.

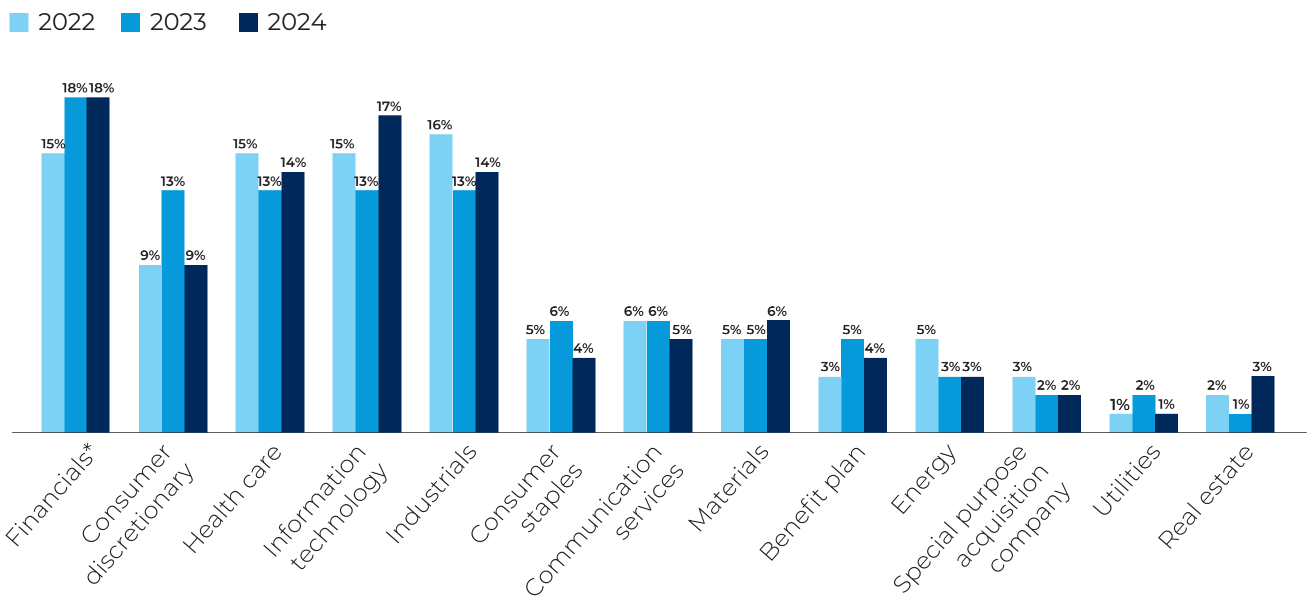
nature, structure, and complexity of the audit, and we consider several factors when evaluating all the engagements we may select. These factors can include economic trends, industry, market capitalization, and prior inspection history.

Figure 4 – Selection Method for Audit Engagements (Annual Firms Only)



We followed the Global Industry Classification Standards (GICS), as reported by S&P Global Ratings, to categorize our inspection reporting by industry.

Figure 5 – Audit Engagements Inspected by Industry Sector

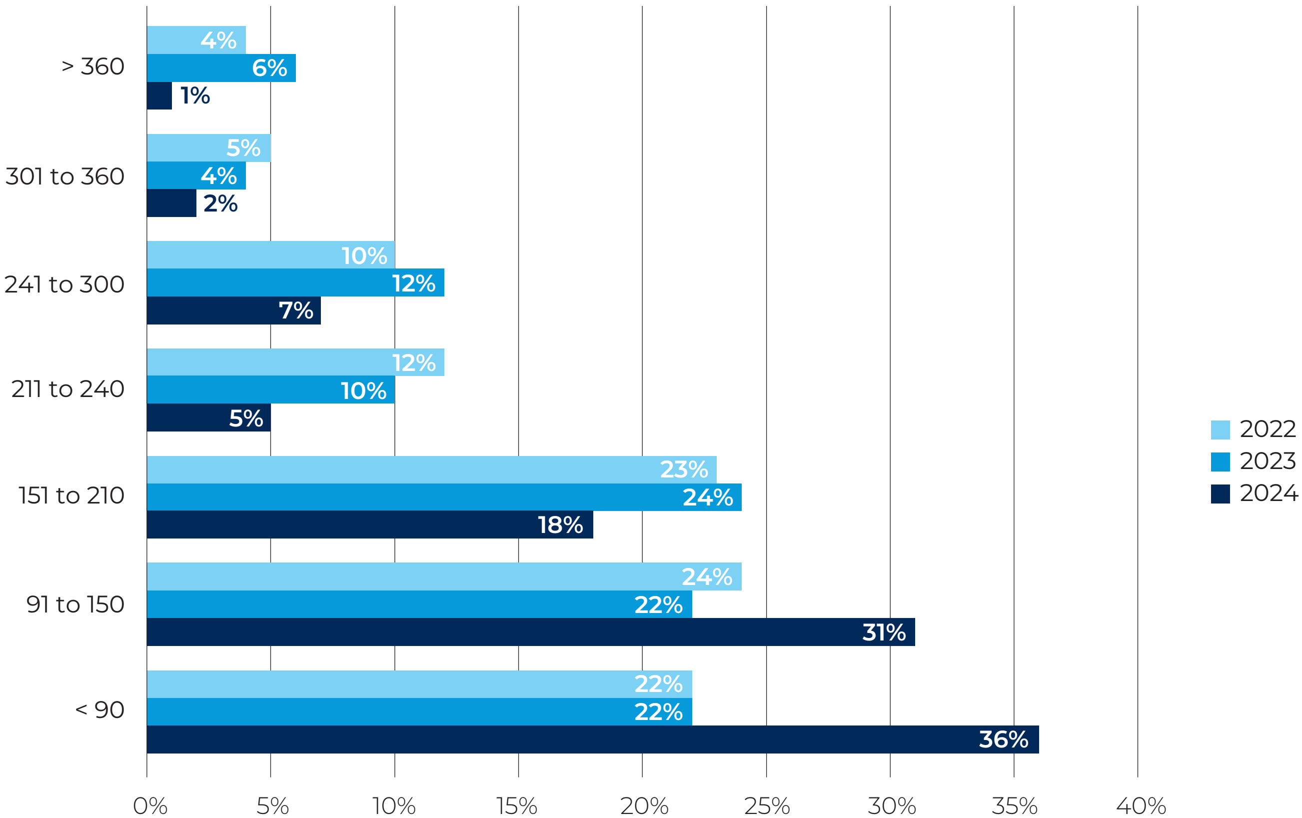


* The Financials GICS sector includes industry classifications for companies engaged in Banking, Financial Services, Consumer Finance, Capital Markets, and Insurance activities. It also includes Financial Exchanges & Data and Mortgage Real Estate Investment Trusts. Within this GICS category, we consider public companies that account for loan losses and take deposits from customers to be a bank for purposes of our inspection reporting. Certain public companies also account for loan losses because they finance purchases, however, we do not count these as banks.

For the engagements we reviewed in 2024, 2023, and 2022, the mix between integrated audits that require an ICFR report and non-integrated audits which do not require an ICFR report was 59% and 41%, 59% and 41%, and 55% and 45%, respectively. Audits of public companies subject to ICFR audit procedures are primarily in the U.S. and non-U.S. GNF inspection programs. Only accelerated filers that are not emerging growth companies and large accelerated filers (as defined by the SEC) must provide an auditor's report on ICFR.

Figure 6 illustrates the time between the date of the auditor's report and our first day of inspection fieldwork, for engagements selected for review:

Figure 6 – Inspections Relative to Audit Report Date (Days Between Report Date and Inspection)



A complete and final set of audit documentation[8] should be assembled for retention as of a date not more than 45 days after the report release date (documentation completion date). Not all firms use the full 45-day period and therefore, in those cases, our inspections can start as soon as the firm informs us the final set of audit documentation has been assembled for retention. Most inspections are performed within seven months of the report release date. Inspections performed after 301 days are mostly related to non-U.S. firms with only one public company audit or our decision to select a prior period audit to be unpredictable.

International Financial Reporting Standards

Most inspections are performed on audits of public companies that follow U.S. Generally Accepted Accounting Principles (U.S. GAAP). The PCAOB also conducts many non-U.S. inspections, where the public company is domiciled outside the U.S. and follows Accounting Standards as issued by the International Accounting Standards Board (IASB). For these audits, we assign staff members who have additional IFRS training; many of the assigned staff have certifications in IFRS. For inspection cycles 2024, 2023, and 2022, inspections where the basis of accounting was IFRS constituted 15%, 14%, and 12% of total engagements inspected, respectively.

[8] In connection with the adoption of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, the Board accelerated the period in AS 1215, *Audit Documentation*, to assemble a complete and final set of audit documentation for retention from 45 days to 14 days, with a two-year phase-in. This change enables PCAOB inspections staff earlier access to audit documentation and reduces the window of opportunity for improper alteration of audit documentation prior to the documentation completion date.

Under amended AS 1215.15, prior to the report release date, (i) the auditor must have completed all necessary auditing procedures and obtained sufficient evidence to support the representations in the auditor's report, and (ii) the engagement partner and other engagement team members performing supervisory activities must have completed their reviews of audit documentation. A complete and final set of audit documentation should be assembled for retention (i.e., archived) as of a date not more than 14 days after the report release date (documentation completion date). If a report is not issued in connection with an engagement, then the documentation completion date should not be more than 14 days from the date that fieldwork was substantially completed. If the auditor was unable to complete the engagement, then the documentation completion date should not be more than 14 days from the date the engagement ceased. The 14-day documentation completion date requirement is effective as follows: a) For public accounting firms that, during the calendar year ending December 31, 2024, issued audit reports with respect to more than 100 issuers, the 14-day documentation completion requirement is effective for audits of financial statements for fiscal years beginning on or after December 15, 2024; and (b) For all other registered public accounting firms, the 14-day documentation completion requirement is effective for audits of financial statements for fiscal years beginning on or after December 15, 2025.

For quarterly reviews conducted pursuant to the standards of the PCAOB, the effective date for the 14-day documentation completion date requirement will begin with the first quarter ending after the first financial statement audits covered by this requirement.

Randomly Selected Engagements

In 2024, 76% of the randomly selected public company audit engagements resulted in at least one deficiency, versus 67% in 2023. We expect approximately 19% of those randomly selected engagements in 2024 will be included in Part I.A, compared to 39% in 2023, and the remainder of the 76% will be included in Part I.B or Part 1.C.

Risk-Based Selection Engagements

In comparison, 74% and 67% of our risk-based public company audit selections in 2024 and 2023, respectively, resulted in at least one deficiency, and we expect approximately 37% and 40% of those risk-based selected engagements will be included in Part I.A, and the remainder of the 74% will be included in Part I.B or Part 1.C.

Focus Areas

Once an engagement is selected for review as part of an inspection, we select portions of the audit, known as "focus areas" for our review. Our considerations when selecting focus areas in 2024 included:

1. Recurring deficiencies
2. Evaluating audit evidence obtained by the auditor
3. Auditor's understanding of the company and its environment
4. Use of other auditors
5. Going concern
6. Critical audit matters

In addition to more traditional focus areas like revenue and business combinations, we might also select non-traditional focus areas. A non-traditional focus area generally varies by audit firm, has not been frequently reviewed in the past, is an area of the audit where a firm has not had a recent QC criticism, and/or is subject to a risk of material misstatement. We vary our selection of non-traditional focus areas on engagements each year to observe how areas of an audit that may be less complex, and more routine, are performed. During 2024, 2023, and 2022, 10%, 15%, and 14%, respectively, of our non-traditional focus areas inspected on public company audits resulted in a deficiency. These deficiencies are all expected to be included in Part I.A of the applicable inspection report and are largely concentrated in the following areas: accruals, debt, equity, and expenses.

II. COMMON DEFICIENCIES

Our findings, presented as examples, on audit deficiencies in this section can include terms unfamiliar to individuals not in the audit profession. Please see "Staff Update on 2023 Inspection Activities" under the Common Deficiencies heading for additional information that may be helpful to better understand our inspection process. Most of the examples of common deficiencies included here are also included in our 2023 Staff Update because they were common deficiencies identified during both years' inspections. We believe that understanding why each example is a deficiency can improve audit quality and, as such, warrants continued emphasis.

Deficiency Examples in Auditing ICFR

An integrated audit of financial statements and ICFR can benefit investors because the auditor's reports address both the audited financial statements and the effectiveness of the controls the public company uses to produce its financial statements. Appropriate application of the top-down, risk-based approach pursuant to PCAOB standards can result in an effective ICFR audit without redundancy.

The following are examples of deficiencies staff frequently observe in ICFR audits grouped by topic area:

Risk Assessment and the Audit of Internal Control

- The engagement team did not appropriately assess the risks of material misstatement related to an important assumption used in an estimate and, as such, the audit response for control testing was not appropriate.
- The engagement team did not appropriately assess the risk of material misstatement related to the valuation of investment securities and the amortization of premiums and discounts related to investment securities and, as such, did not identify the risk of material misstatement and performed no control testing over this aspect of the control.
- The engagement team did not reevaluate and revise its initial risk assessment after it obtained audit evidence during the audit that contradicted the audit evidence on which it originally based its risk assessment. Because the team did not reevaluate and revise its initial risk assessment in light of the new audit evidence, the audit response for control testing was not appropriate.

Selecting Controls To Test

- Particularly for smaller public companies, the engagement teams did not identify and test controls that addressed the risk that the same individual could prepare and post journal entries in the general ledger system without approval or any other oversight or compensating control.
- The engagement team did not identify and test controls over the accuracy and completeness of a significant calculation that was used in the performance of a key control in multiple financial statement areas including allowance for credit losses, inventory, accruals, and accounts impacted by business combinations.

Testing Design Effectiveness

- The engagement team did not sufficiently test the design effectiveness of a control because it did not evaluate the effect of incomplete information available to the control owner and, as such, the ability of the control, as designed, to effectively prevent or detect a material misstatement.

Testing Management Review Controls

- The engagement team did not evaluate the specific review procedures that the control owner performed to assess the reasonableness of assumptions used in the valuation of securities.
- The engagement team did not test the aspects of the control that addressed whether the method used by the public company to develop the estimates subject to management review were in conformity with the applicable financial reporting framework.
- The engagement team did not evaluate the specific review procedures the

control owner performed to evaluate the reasonableness of the projected amounts for revenue growth and costs that the public company used in its impairment analysis.

IT Considerations, Including System-Generated Data and Reports

- The engagement team did not identify and test controls over the accuracy and completeness of the reports used in the operation of a control as they relied on information that originated from the system.

Rolling-Forward Controls Tested at an Interim Date

- The engagement team tested operating effectiveness as of an interim date and did not perform any procedures, including inquiries, during the period from the interim testing until year-end.

Using the Work Of Others

- The engagement team did not evaluate whether it had a reasonable basis for using the work of internal audit as audit evidence of the operating effectiveness of selected controls given the increased risk associated with the controls.

Using the Work Of Other Auditors[9]

- The component engagement team did not fulfill the objectives of its role in an audit in which it was not the principal auditor because it did not identify and test appropriate controls related to assertions specifically identified by the principal auditor as important in the instructions to the component firm.

Evaluating Identified Control Deficiencies

- The engagement team did not sufficiently evaluate whether the deficiencies identified in controls represented a material weakness because it did not identify that the compensating controls did not address all the risks the primary control was designed to detect related to inaccurate and unauthorized sales orders and prices.
- The engagement team did not sufficiently evaluate the severity of the identified deficiencies to determine whether these deficiencies, individually or in combination with other deficiencies, constituted a material weakness.
- The engagement team did not communicate to the public company's management, in writing all deficiencies in ICFR identified during the audit prior to the issuance of the audit report.

[9] Effective for audits of financial statements for fiscal years ending on or after December 15, 2024, the PCAOB amended or adopted standards to strengthen requirements for planning and supervising audits involving accounting firms and individual accountants outside the accounting firm that issues the auditor's report. Please see the following:

- AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*
- AS 1201, *Supervision of the Audit Engagement*
- AS 1206, *Dividing Responsibility for the Audit with Another Accounting Firm*
- AS 1215, *Audit Documentation*
- AS 1220, *Engagement Quality Review*
- AS 2101, *Audit Planning*

AS 1205, *Part of the Audit Performed by Other Independent Auditors*, was rescinded.

Deficiency Examples in Auditing Financial Statement Areas

The top categories, in terms of financial statement area, remain relatively consistent year-to-year, and significant estimates, evidence, and/or data and reports used to support audit conclusions are often a component. In April 2024, we published, "Inspection Observations Related to Auditor Use of Data and Reports."

Accounting estimates are found throughout the financial statements. By their nature, accounting estimates, including fair value measurements, generally involve subjective assumptions and measurement uncertainty, making them susceptible to management bias. Some estimates involve complex processes and methods. As a result, financial statement accounts with accounting estimates are often some of the areas of greatest risk in an audit, requiring additional audit attention and appropriate application of professional skepticism. The challenges of auditing estimates may be compounded by cognitive bias, which could lead auditors to anchor on management's estimates and inappropriately weight confirmatory over contradictory evidence. In Figure 7, we show the reason a comment form was issued, by firm category, related to estimates and assumptions of all financial statement accounts. As with the following figures in this section, the legend descriptions can be mapped to the related audit standard.

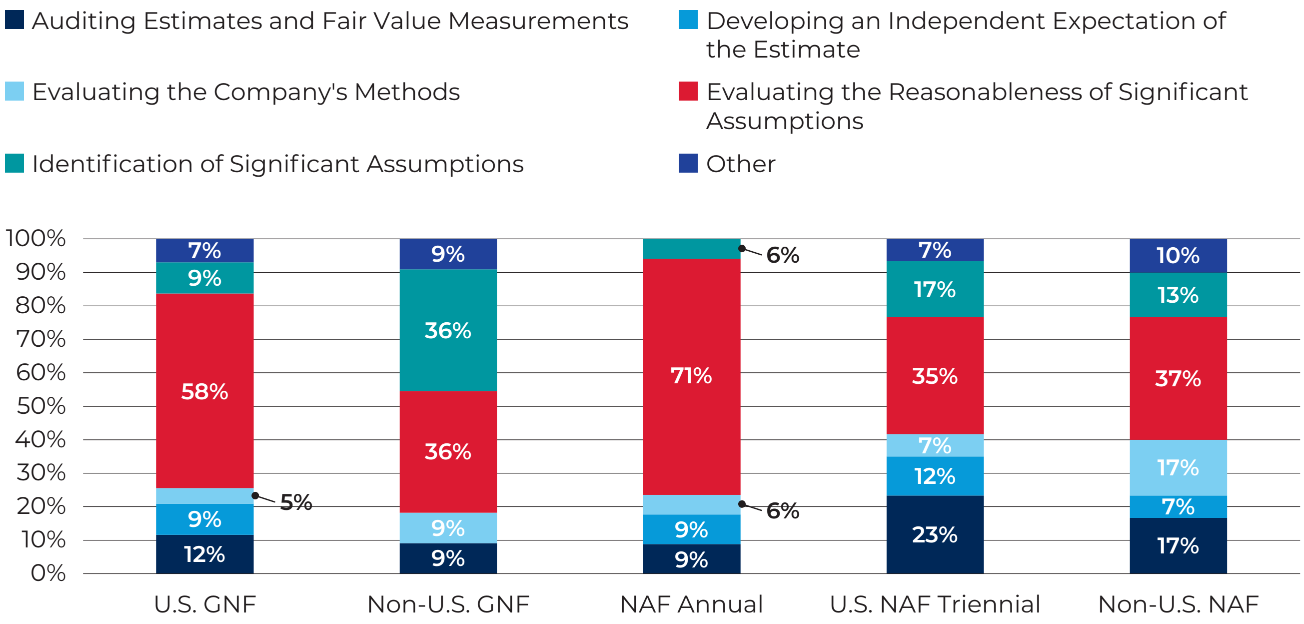
Top Financial Statement Area Deficiency Categories

- Revenue and revenue related accounts
- Inventory
- Accounts impacted by business combinations
- Investment securities
- Allowance for credit losses
- Long-lived assets, goodwill, and intangible assets

Failures to properly test accounting estimates, including fair value measurements, result in deficiencies in many financial statement accounts, including several listed above.

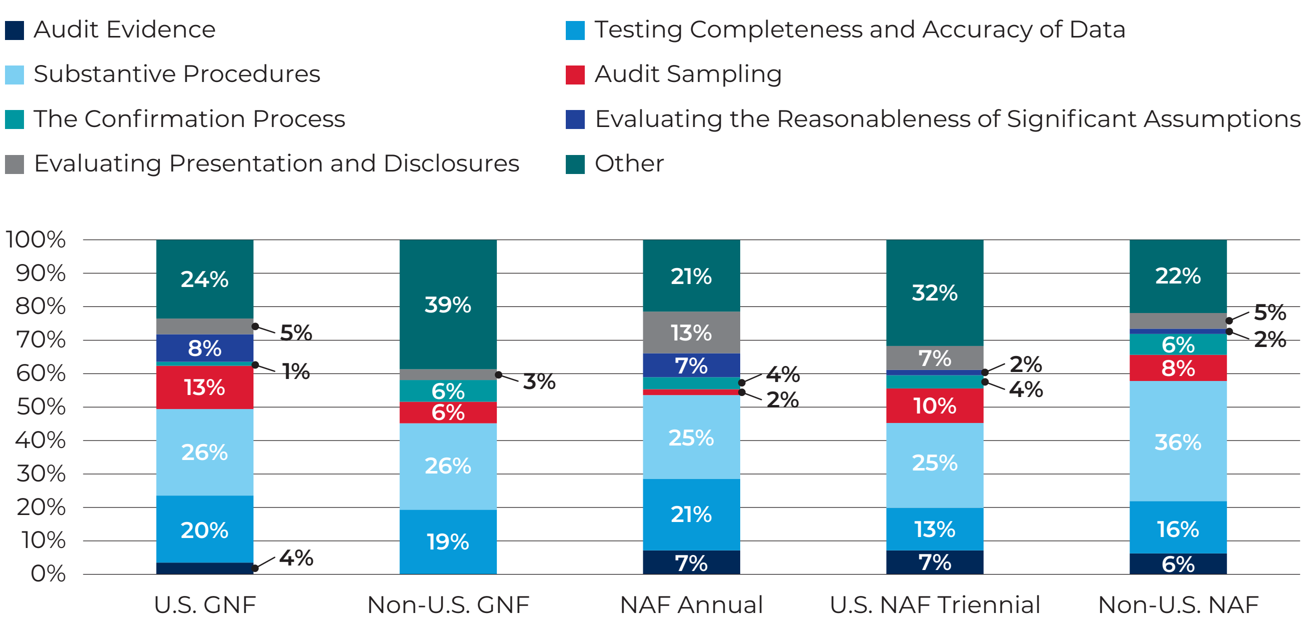
We observed deficiencies across a broad range of financial statement accounts and transactions related to accounting estimates. Our most common observations related to accounting estimates and significant assumptions are (1) revenue recognition, such as standalone selling price, (2) accounts impacted by business combinations, including fair value and contingencies, and (3) forecasted information used to evaluate potential impairments or calculated fair value.

Figure 7 – Estimates and Assumptions – Deficiencies by Audit Standard Cited



Revenue and Revenue Related Accounts

Figure 8 – Revenue and Revenue Related Accounts – Deficiencies by Audit Standard Cited

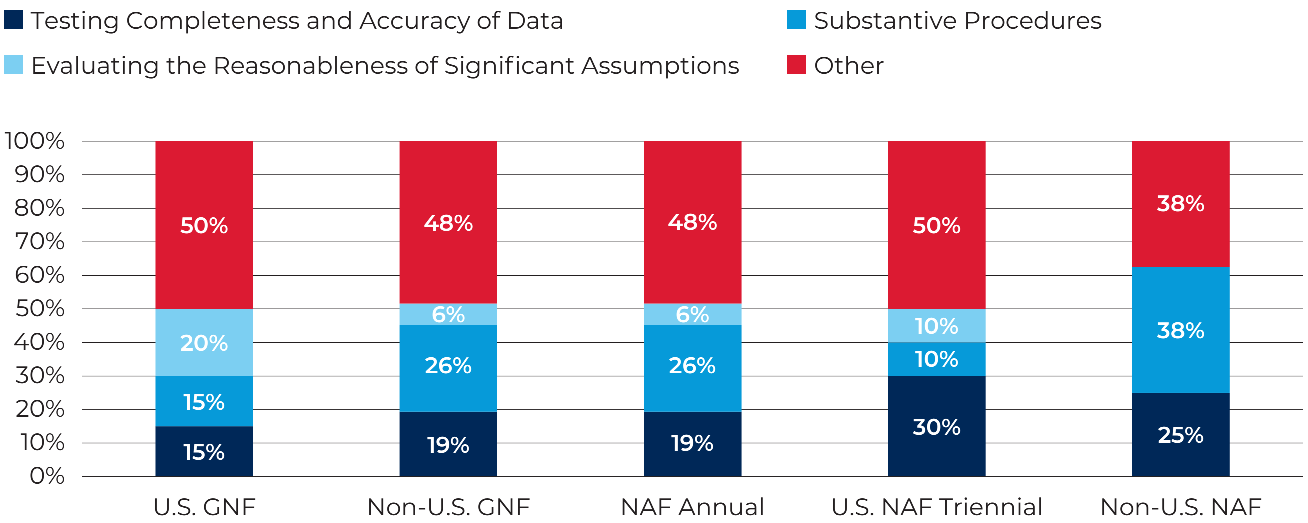


Revenue, often a key metric to a public company's financial performance, is a frequently selected focus area in our inspections given, among other things, (1) complexities often associated with revenue recognition accounting policies and practices and (2) complexities associated with the auditing of such policies and practices. The following are examples of deficiencies staff observed. The engagement team did not:

- Perform sufficient procedures to test disaggregated revenue presentation and disclosure.
- Perform appropriate and/or sufficient procedures to evaluate data used in a software-assisted correlation analysis (an analysis that shows the level of correlation between specified factors, such as certain costs and revenue recognition). In some instances, the engagement team even identified data in their analysis that did not relate to revenue, but did not evaluate the implication of that finding to their testing, resulting in the engagement team not performing sufficient procedures to address the occurrence, allocation, and completeness of revenue.
- Perform sufficient procedures related to valuation and allocation of bundled sales transactions to test that those sales transactions were recorded at relative stand-alone selling prices.
- For accounts receivable, perform confirmation testing for existence or occurrence, or document how they overcame the presumption to perform confirmation procedures.
- Perform any procedures on significant assumptions in a percentage of completion basis of revenue recognition.
- Test whether the public company's arrangements to provide multiple services as one distinct performance obligation recognized over time had been satisfied before revenue was recognized.
- Test the accuracy and completeness of historical data used in testing procedures related to current year transactions.
- Identify or overcome the presumption of fraud risk involving improper revenue recognition.
- Select a sample that could be expected to be representative of each product revenue population.

Inventory

Figure 9 – Inventory – Deficiencies by Audit Standard Cited

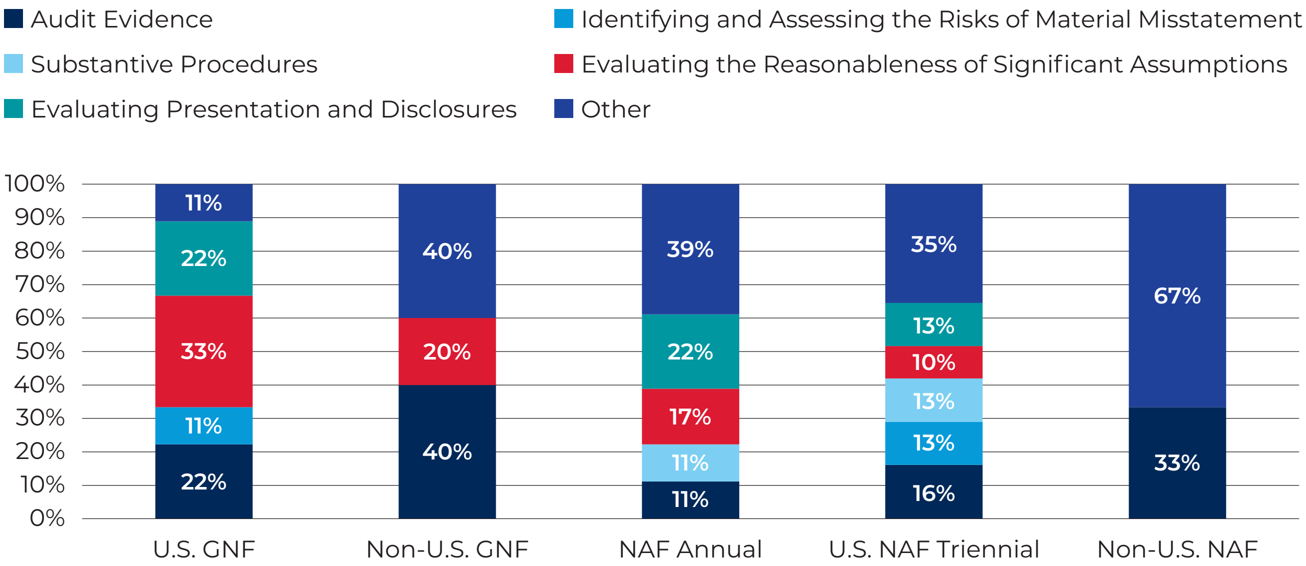


Inventory can often present a significant risk of material misstatement due to the complexities of determining the cost of inventory and measuring inventory on-hand at a point in time. The following are examples of deficiencies staff observed. The engagement team did not:

- Perform any procedures to test the accuracy and completeness of the period-end inventory listing reports and the completeness of the physical inventory adjustments used in the testing of the existence of inventory.
- Perform appropriate procedures to test inventory movement between the interim date and period-end date when the physical inventory observation is as of the interim date.
- Perform price testing of old inventory or otherwise evaluate management's assessment and accounting for old inventory.
- Obtain sufficient appropriate audit evidence that the public company's cycle count procedures over inventory were sufficiently reliable to produce results substantially the same as those that would have been obtained by a count of all items at a point in time.
- Perform any testing of the valuation of inventory (whether inventory was recorded at the lower of cost or net realizable value).
- Perform sufficient substantive procedures to test the completeness, existence, and valuation of inventory held at the public company's subsidiary because the engagement team limited its procedures to reviewing the public company's inventory reconciliation.

Accounts Impacted by Business Combinations

Figure 10 – Accounts Impacted by Business Combinations – Deficiencies by Audit Standard Cited

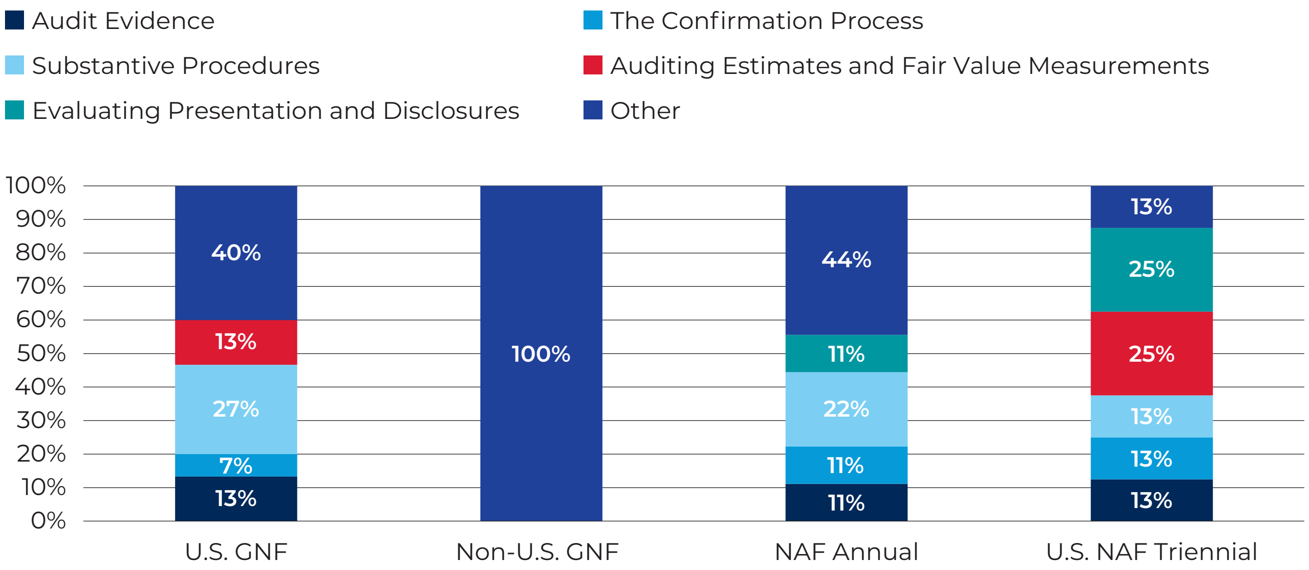


Business combinations, by their nature, impact many accounts and include a broad spectrum of accounting estimates, including fair value, and many of our observations are included above under Deficiency Examples in Auditing ICFR, particularly testing management review controls. The following are additional examples of the deficiencies staff observed. The engagement team did not:

- Perform sufficient substantive procedures to test valuation and allocation of purchase accounting, including forecast information used in valuations.
- Perform sufficient substantive procedures to test other significant aspects of the acquisition agreement such as contingent consideration.

Investment Securities

Figure 11 – Investment Securities – Deficiencies by Audit Standard Cited

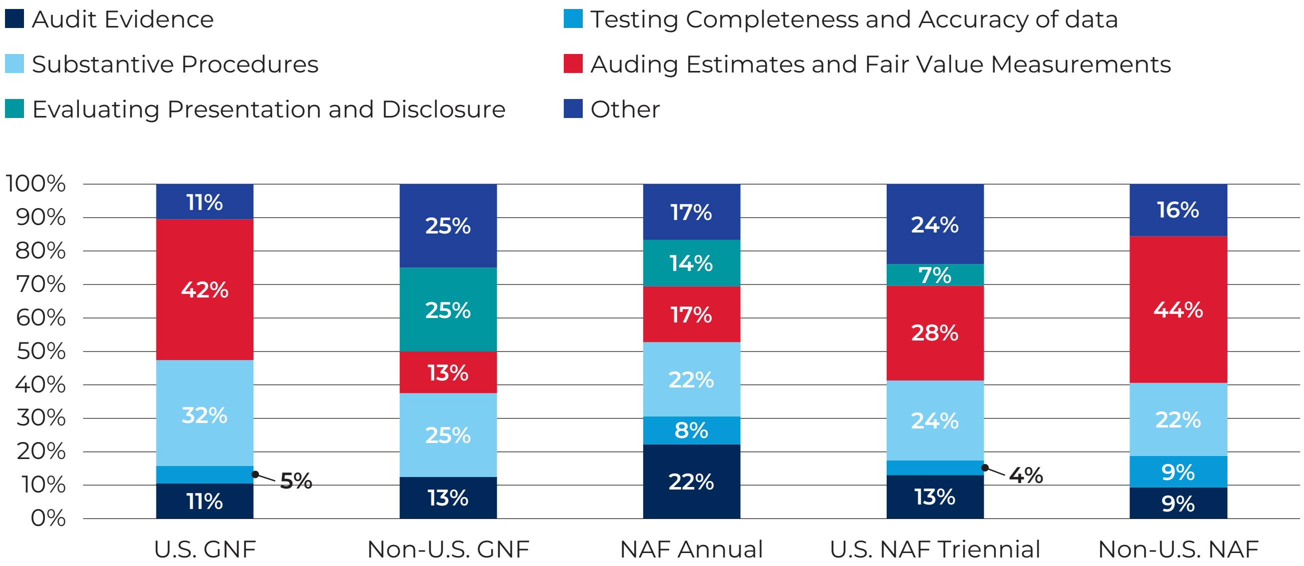


Investment securities usually represent the second largest asset class for banks. Key risks presented by investments include interest rate risk, market risk, liquidity risk, and credit risk. The following are examples of deficiencies staff observed. The engagement team did not:

- Perform sufficient substantive procedures to test the fair value hierarchy presentation and disclosures in the notes to the financial statements.
- Obtain an appropriate sample for testing the investments that could be expected to be representative of each population of investments.
- Perform any substantive procedures to test assumptions used in the valuation of investments.

Long-lived Assets, Goodwill, and Intangible Assets

Figure 12 – Long-lived Assets, Goodwill, and Intangible Assets – Deficiencies by Audit Standard Cited

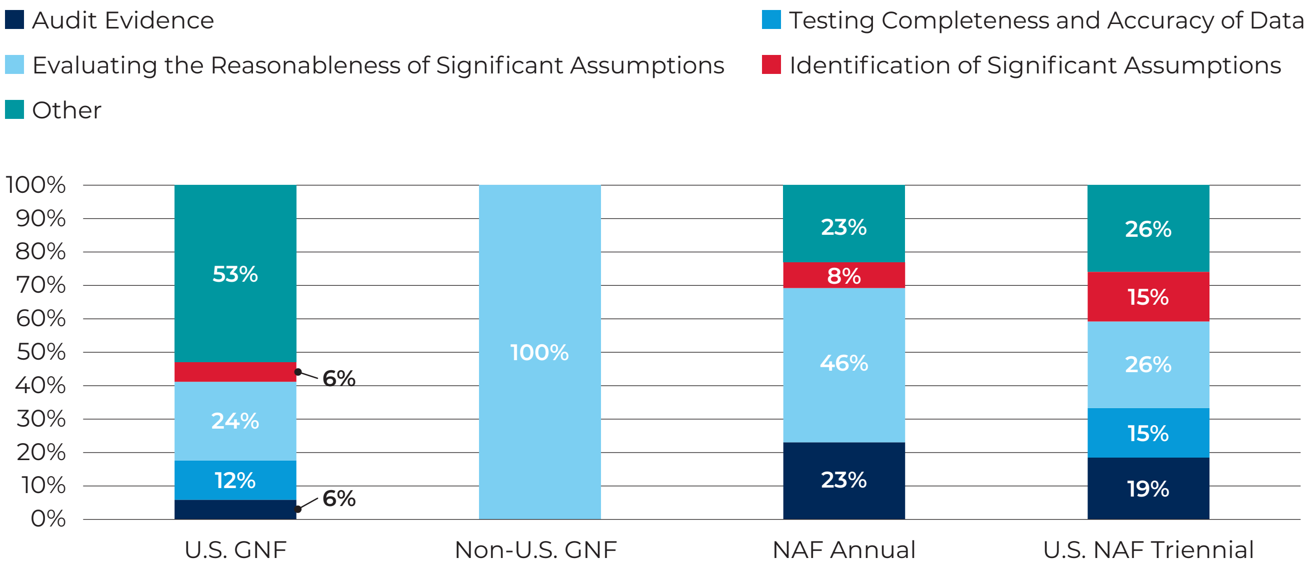


The valuation of long-lived assets requires considerable judgment and professional skepticism, and an appropriate assessment of the risks of material misstatement at the financial statement level and the assertion level. The process to assess whether an impairment exists is often complex and includes both qualitative and quantitative factors. A company's specialist is often used to model a forecast of revenue, operations, or cash flows used to test for impairment and/or determine fair value. The following are examples of deficiencies staff observed. The engagement team did not:

- Perform sufficient procedures with respect to using the work of a company's specialist as audit evidence, specifically testing the accuracy and completeness of information prepared by the public company and used by the company's specialist in developing the estimates and/or evaluating the reasonableness of significant assumptions; and performing procedures to evaluate whether the methods used by the issuer's specialist were appropriate.
- Sufficiently evaluate the valuation of the assets and whether there were indicators of potential impairment.
- Obtain a sufficient understanding of the processes used to develop the accounting estimates for the impairment to appropriately test valuation.
- Evaluate the reasonableness of a forecast period in the cash flow projections used to test present value.
- Identify and evaluate the significance to the financial statements of the public company's omission of certain required disclosures related to goodwill to appropriately test presentation and disclosure.
- Perform any procedures to evaluate the reasonableness of the significant assumptions underlying an estimate, beyond reading the public company's memorandums.

Allowance for Credit Losses

Figure 13 – Allowance for Credit Losses – Deficiencies by Audit Standard Cited



The allowance for credit losses (ACL) represents one of the most significant accounts for financial institutions and involves significant management judgment incorporated into models that can be very complex. In September 2024, we published, "Bank Financial Reporting Audits" to assist auditors as they were performing their audits of financial institutions. The following are examples of deficiencies staff observed. The engagement team did not:

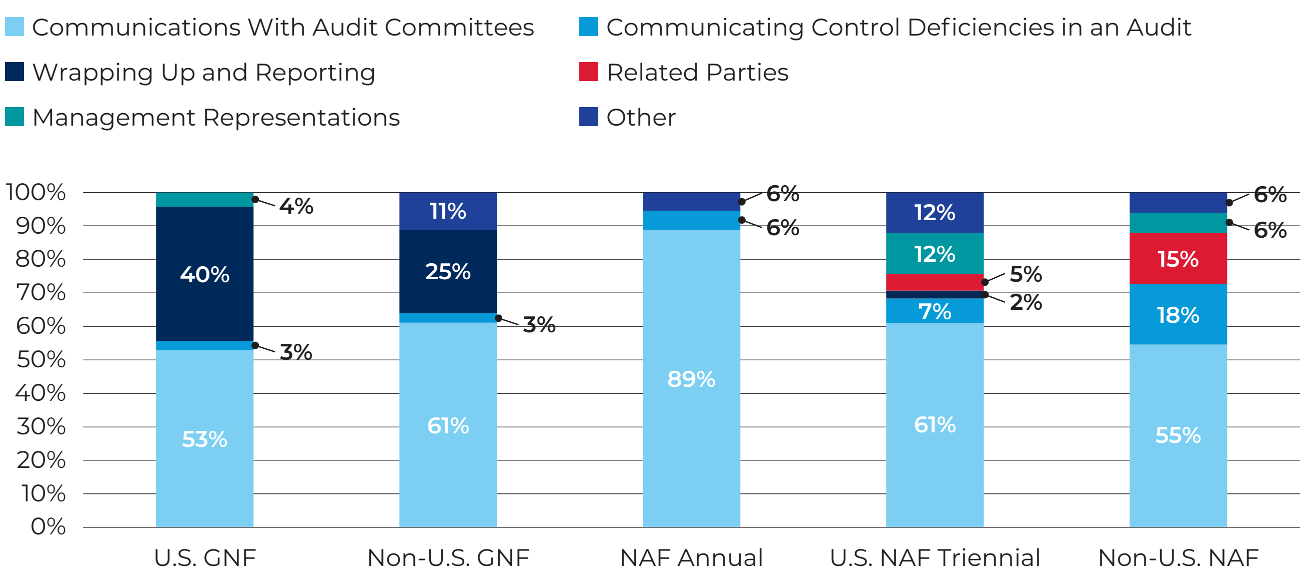
- Sufficiently test the reasonableness of commercial loan risk ratings. Specifically, the engagement team did not select an appropriate sample that could be expected to be representative of the total loan population because the engagement team did not appropriately consider the characteristics of the population.
- Evaluate whether the public company's valuation methodologies used in their purchase price allocation were in conformity with the requirements of the applicable financial reporting framework.
- Sufficiently test the completeness and accuracy of reports that support significant assumptions and are used in the engagement team's testing of the ACL valuation.
- Perform any procedures to identify assumptions used to develop the unallocated reserve and evaluate the reasonableness of those assumptions as part of their valuation testing.
- Perform sufficient substantive procedures to test the reasonableness of loan grades, a significant input to valuation testing.

Deficiency Examples Related to Other PCAOB Standards or Rules

The Rules of the Board include a variety of topics that can be subject to our inspection activities. We report other instances of non-compliance with PCAOB standards or rules in Part I.B of our inspection reports. These deficiencies relate to instances other than those in which the firm had not obtained sufficient appropriate audit evidence to support its opinion(s). In 2024, the most common Part I.B deficiencies related to (1) audit committee communications and (2) consideration of fraud. For U.S. NAF Triennial firms, deficiencies related to the auditor's reporting model and Form AP were also common.

Audit Committee Communications

Figure 14 – Audit Committee Communications – Deficiencies by Audit Standard Cited



Both the auditor and the audit committee benefit from a meaningful exchange of information throughout the audit to assist in understanding matters relevant to the audit. However, staff continued to identify deficiencies in the required auditor's communication with the audit committee.

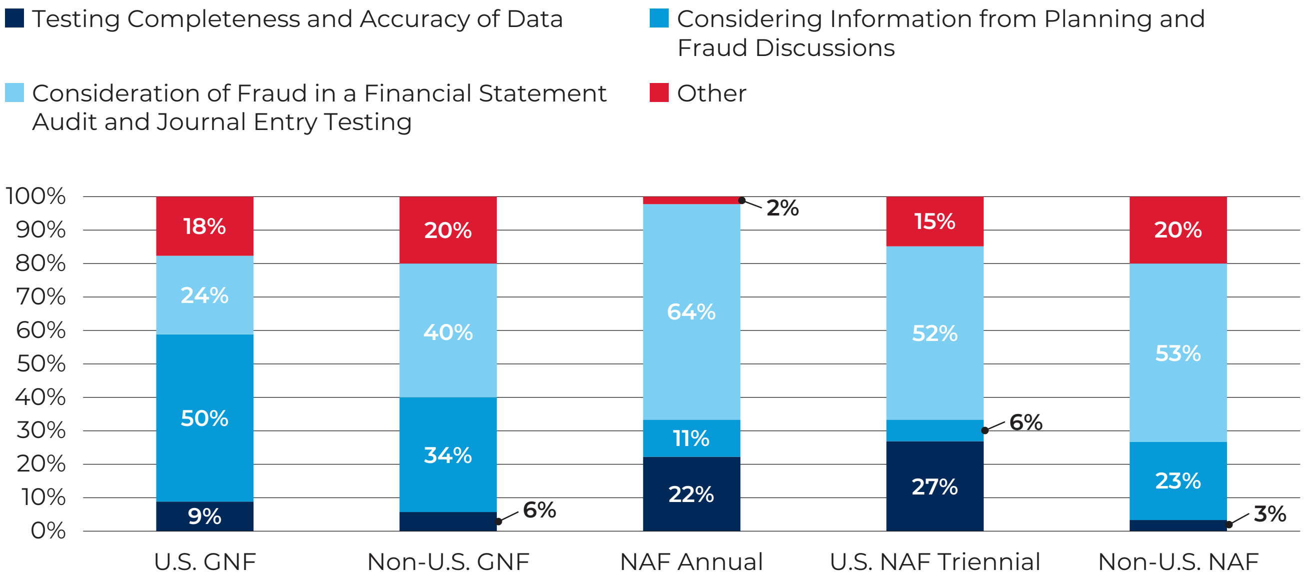
Deficiencies ranged broadly across all types of firms, and the following are examples of deficiencies staff observed. The auditor did not communicate to the public company's audit committee:

- An understanding of the terms of the audit engagement in an engagement letter and determine that the audit committee had acknowledged and agreed to the terms of the engagement.
- The significant risks that were identified during its risk assessment procedures or changes to significant risks that occurred during the year as risk assessment was updated.

- Critical accounting estimates and related significant assumptions with a high degree of subjectivity.
- The names, locations, and planned responsibilities of other independent public accounting firms or other persons, who are not employed by the auditor, that perform audit procedures in the current period audit.
- The management representation letter and/or a complete list of uncorrected misstatements identified during the audit.

Fraud

Figure 15 – Fraud – Deficiencies by Audit Standard Cited



The auditor should perform risk assessment procedures that are sufficient to provide a reasonable basis for identifying and assessing the risks of material misstatement, whether due to error or fraud. An understanding of the public company, its relationships and transactions with related parties, its environment, and its flow of transactions, including how transactions are initiated, authorized, processed, and recorded, better informs the auditor to identify fraud risks and to develop an appropriate audit response.

Material misstatements of financial statements due to fraud often involve the manipulation of the financial reporting process by (a) recording inappropriate or unauthorized journal entries throughout the year or at period end or (b) making adjustments to amounts reported in the financial statements that are not reflected in individual journal entries, such as through consolidating adjustments, report combinations, and reclassifications. Accordingly, the auditor should design procedures to test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of financial statements, such as top-side entries. To do this effectively, the auditor should understand the public company's financial statement close process, including the recurring and automated journal entries.

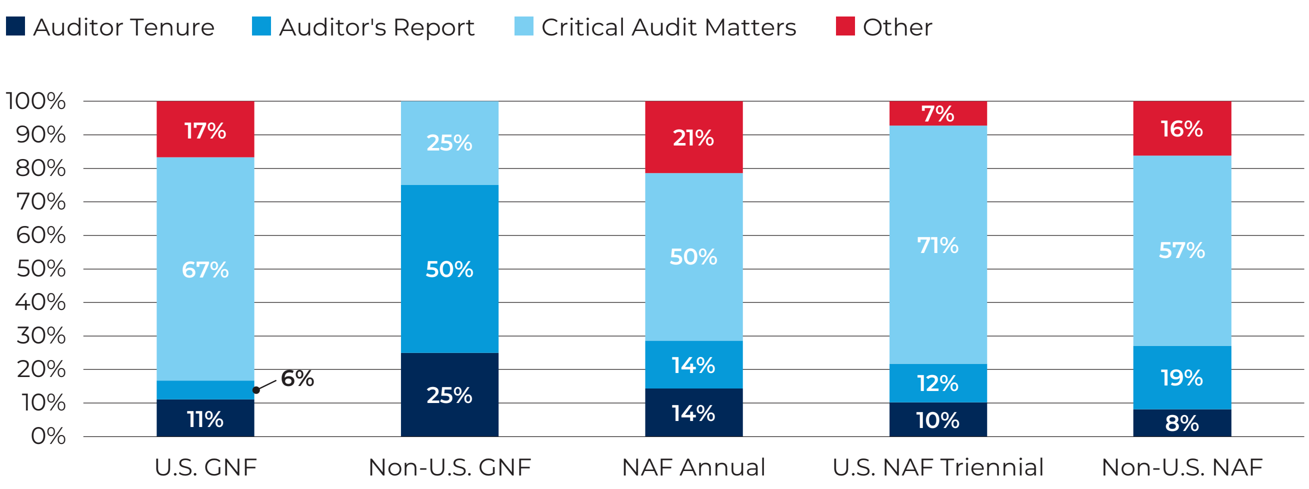
Strong data and analytical skills, which may be supported by technology-driven tools appropriate to the public company's environment, are important for auditors to effectively perform fraud procedures – which should never be viewed as routine requirements that need to be checked to complete a list.

The following are examples of deficiencies staff observed. Depending on the facts and circumstances of these deficiencies, they may appear in Part I.A or Part I.B. The engagement team did not:

- Conduct a brainstorming discussion among the key engagement team members about the potential for material misstatement due to fraud.
- Sufficiently test the completeness of the population that was used to make selections for journal entry testing.
- Perform required inquiries with the audit committee, management, and others within the public company about fraud risks.
- Support its rationale used for identification and selection of journal entries for testing.
- Support its rationale for limiting its testing to only certain journal entries that met its identified fraud criteria.
- Include entries in its journal entry testing that met their fraud risk criteria.
- Examine the underlying support for certain of the journal entries identified based on the risk criteria.
- Perform any procedures to identify and select journal entries and other adjustments for testing.

Auditor's Reporting Model

Figure 16 – Auditor's Reporting Model – Deficiencies by Audit Standard Cited



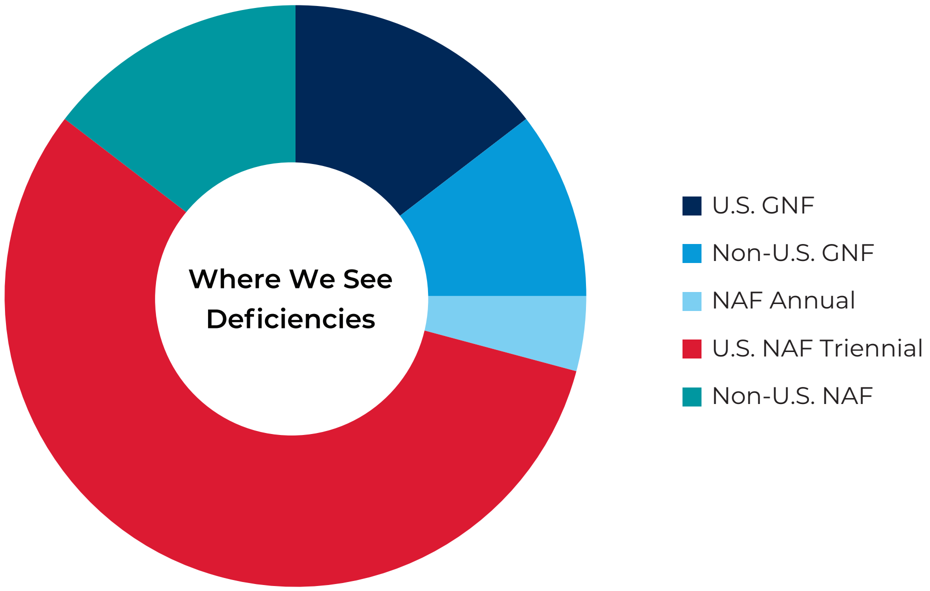
An auditor's communication of critical audit matters (CAMs) in the auditor's report is intended to inform investors and other financial statement users about any matters arising from the audit of the financial statements (1) that were communicated or required to be communicated to the audit committee and that relate to accounts or disclosures that are material to the financial statements and involve especially challenging, subjective, or complex auditor judgment, and (2) the auditor's response to those matters.

The 2024 inspection deficiencies primarily relate to instances in which audit procedures to determine whether or not matters were CAMs did not include every matter that was communicated, or required to be communicated, to the issuer's audit committee and that related to accounts or disclosures that were material to the financial statements. These instances of noncompliance do not necessarily mean that other CAMs should have been communicated in the auditor's report. We also observed instances where the firm did not accurately describe how the CAM was addressed in its audit, because the CAM description in the auditor's report included procedures that were not performed to address the CAM or were not performed as described. In limited instances within the NAF program, staff performing triennial firm inspections found that some auditors performed no procedures regarding CAMs.

The PCAOB has a research project focused on the communication of CAMs. The project seeks to understand why there continues to be a decrease in the average number of CAMs reported by audit firms of all sizes in their auditor's reports over time and whether there is a need for additional guidance, changes to PCAOB standards, or other regulatory action to improve such reporting, including the information that is provided as part of the CAM reporting.

Form AP

Figure 17 – Form AP Deficiencies by Firm Type



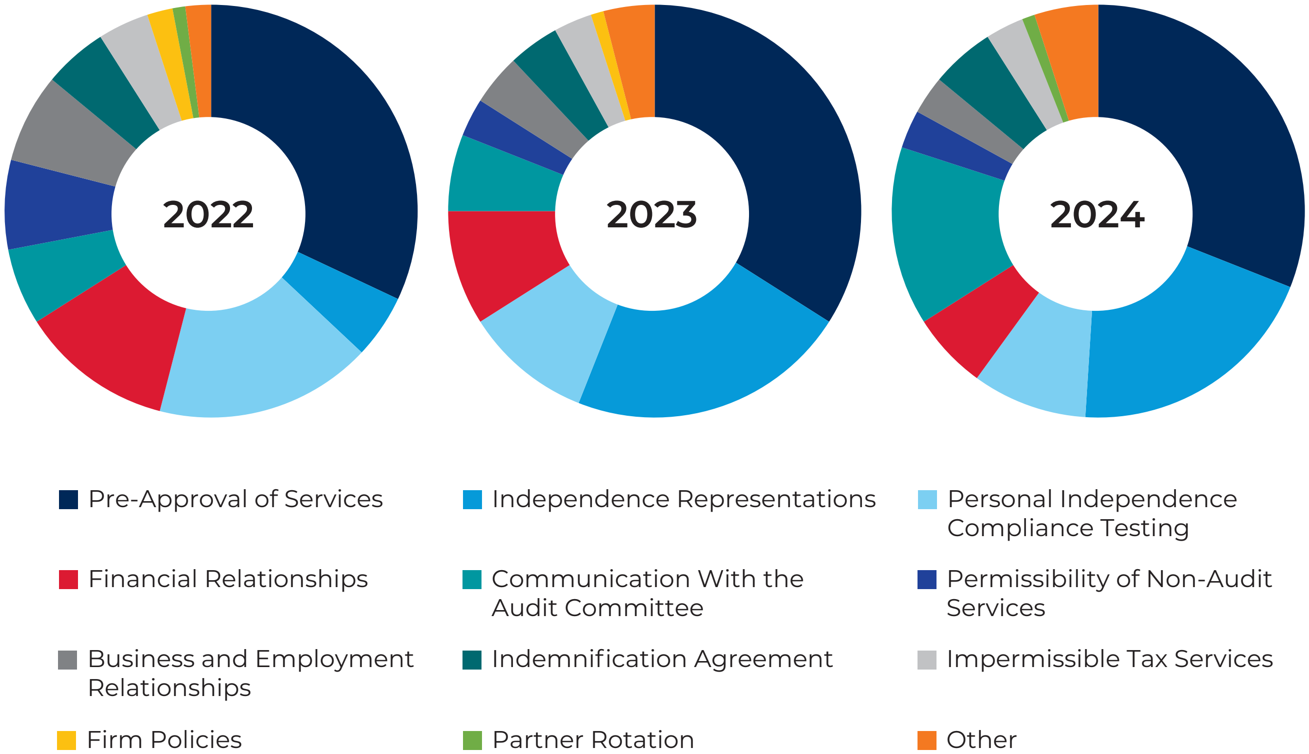
Form AP was adopted to provide investors and other financial statement users with information about engagement partners and accounting firms that participate in audits of public companies. The information is filed on Form AP, Auditor Reporting of Certain Audit Participants, (in accordance with Rule 3211) and is available in the searchable AuditorSearch database on the PCAOB website. We continue to observe instances of incomplete or inaccurate information being reported as well as delinquent filings. The form is due by the 35th day after the date the audit report is first included in a document filed with the SEC. In March 2025, we published, "Audit Focus: Form AP," which we encourage you to read.

Deficiency Examples Related to Independence

Independence, reported in Part I.C, remains an area for improvement. Instances of potential noncompliance with SEC rules or instances of noncompliance with PCAOB rules, regardless of the means of identification of the deficiency (by the PCAOB or reported to us by the firm) remain fairly consistent year-to-year. Compliance by all personnel and partners with a firm's process to preserve independence, in fact and in appearance, from the public companies they audit is fundamental to a strong culture of integrity and audit quality.

We identify (including firm self-reported instances) potential violations of the SEC's independence requirements. These potential violations, mainly with triennially inspected audit firms (which includes non-U.S. GNF), include financial relationships, employment relationships, business relationships, permissibility of non-audit services, contingent fees, and audit committee pre-approval of services. Some of the annually inspected firms continue to report a high rate of noncompliance by audit firm personnel reporting their financial relationships in

Figure 18 – Independence-Related Comment Forms



accordance with firm policies (which includes matters that go beyond the SEC and/or PCAOB rules and include reporting deadlines) that could be more restrictive than the SEC or PCAOB independence requirements, in the applicable audit firm's monitoring system. We also observed deficiencies related to PCAOB Rule 3524, *Audit Committee Pre-approval of Certain Tax Services*.

A public company may be particularly interested in their auditor's potential noncompliance with SEC and PCAOB independence rules, as the auditor independence requirements underpin the public company's requirement to file financial statements audited by an independent registered public accounting firm. In September 2024, we published, "Inspection Observations Related to Auditor Independence," highlighting staff observations on independence, including a description of each category of observations noted in Figure 18 above, and detailed examples of common deficiencies.

III. OBSERVATIONS RELATED TO QUALITY CONTROL SYSTEMS

Quality Control Criticisms

Effective QC systems are crucial for consistent high-quality audits and other engagements under PCAOB standards.

Part II of the inspection report includes criticisms of, or potential defects in, the firm's QC system. Section 104(g)(2) of the Sarbanes-Oxley Act restricts the PCAOB from publicly disclosing Part II deficiencies unless the firm does not address the criticisms or potential defects to the Board's satisfaction no later than 12 months after the issuance of an inspection report. A reader should not infer from any Part I deficiency, or combination of deficiencies, that a QC finding is identified in Part II.

Our inspections assess the degree of compliance of each registered public accounting firm and associated persons of that firm with the Board's rules, the rules of the SEC, and professional standards. The inspection of a firm's QC system, along with the review of issuer audits, is integral to this purpose.

Our current QC procedures, which may change once QC 1000[10] becomes effective, generally consist of:

1. Gaining and/or updating an understanding of the design of the firm's QC system;
2. Performing element-specific and/or firm-specific inspection procedures related to the effectiveness of certain QC elements; and
3. Considering other available information that may provide evidence of the effectiveness of the QC system.

In 2025, we will also begin collecting information to understand the firm's readiness for QC 1000.

The inspection process for a firm's QC system consists of core procedures and supplemental information gathering procedures.

If identified deficiencies, when accumulated and evaluated, indicate sufficiently significant defects or potential defects in the firm's system of quality control, the PCAOB inspection report will include a discussion of those issues as a QC criticism.

Determining whether a QC criticism exists involves evaluating inspection findings individually and in the aggregate. Our objective is to ensure the consistent evaluation of the results of a firm's inspection. We also consider

[10] QC 1000, *A Firm's System of Quality Control*, and related amendments to PCAOB standards, rules, and forms will be effective as of December 15, 2025. QC 1000 replaces the PCAOB's interim QC standards.

finding-specific factors such as the nature of the criticism or the potential criticism underlying the inspection finding and firm-specific factors that relate to various aspects of the firm's audit practice and the QC system (such as firm methodology, similar findings, and inspection history). Implicit in the finding-specific factors and firm-specific factors, we consider the magnitude and likelihood of the finding(s). Magnitude relates to the nature and severity of the finding, and likelihood relates to the possibility of other occurrences of the inspection finding(s).

The following are examples of QC criticisms related to a firm's system of QC found in 2024:

- **Testing controls.** The inspection results indicate that the firm's system of QC does not provide reasonable assurance that the work performed by the firm's personnel with respect to testing controls will meet the requirements of AS 2201 and AS 2301. (QC 20.03 and .17)

  Addressing these concerns and monitoring the effects of the actions taken regarding testing controls are critical because (1) the results of these procedures are used to support the firm's opinion on the effectiveness of ICFR and (2) control reliance is often used as the basis for modifying the nature, timing, and extent of substantive testing in audits of financial statements.

- **Reliance on data or reports.** The inspection results indicate that the firm's system of QC does not provide reasonable assurance that the work performed by the firm's personnel to establish a basis for reliance on data or reports will meet the requirements of AS 1105, AS 2201, and AS 2301. (QC 20.03 and .17)

- **Supervision of the audit.** The inspection results indicate that the firm's system of QC does not provide reasonable assurance that the supervisory activities, including reviews of audit work, performed by the firm's engagement partners will meet the requirements of AS 1201. (QC 20.03 and .17)

- **Engagement quality review.** The inspection results indicate that the firm's system of QC does not provide reasonable assurance that the review procedures performed by the firm's engagement quality reviewers will meet the rquirements of AS 1220. (QC 20.03 and .17)

- **Policies for financial holdings disclosures.** The inspection results indicate that the firm's system of QC does not provide reasonable assurance that the firm and its personnel will comply with the firm's policies and procedures with respect to independence-related regulatory requirements. (QC 20.04, .09, and .10)

Remediation

During 2024, the Board made remediation determinations related to 101 firm inspection reports. On average, these firms provided two draft responses during the remediation period with respect to which staff provided feedback to the respective firms. The Board reached a satisfactory determination for each of the quality control criticisms included in inspection reports for approximately 66% of the 2024 remediation determinations ("fully satisfactory determination").

For the remaining approximately 34% of the 2024 remediation determinations, the Board determined that each firm did not satisfactorily remediate one or more of the quality control criticisms included in the firm's inspection report ("unsatisfactory determination"). The areas of QC with an unsatisfactory determination by the Board most frequently related to (1) engagement quality review, (2) policies for financial holdings disclosures and other independence matters, (3) testing controls, (4) supervision of the audit, and (5) auditor reporting of certain audit participants.

In 2023, we issued a Spotlight providing additional insights on the remediation process. During 2024, we provided more guidance concerning the remediation process and continued to encourage open and frequent, two-way communication between the audit firms and the PCAOB during the remediation process.

IV. AREAS WITH RECURRING DEFICIENCIES, 2022 TO 2024 INSPECTIONS

Firms that have repeated or persistent criticisms should thoughtfully consider why and make meaningful changes where appropriate. The inspection staff believes that a firm's analysis of the root cause(s), although not currently required, may be helpful in determining appropriate actions to remedy repeated or persistent criticisms from our inspections. In April 2024, to help smaller firms better understand the underlying root causes of a deficiency, we published, "Root Cause Analysis – An Effective Practice To Drive Audit Quality." The nature and extent of the root cause process will likely differ significantly with a firm's size and structural complexity.

Deficiencies in Auditing ICFR

Deficiencies in auditing ICFR were related to the sufficiency and appropriateness of audit evidence supporting an audit firm's ICFR opinion. These deficiencies represent instances of noncompliance with AS 2201 observed in our testing of issuers.

The three-year data highlights the nature of ICFR auditing deficiencies and deficiencies in auditing ICFR by area that have generated the most comment forms since 2022. The data in Figure 20 related to the nature of ICFR can total more than 100% because comment forms can contain multiple deficiencies. Figure 20 presents the deficiencies by audit area using the number of times the audit area was selected for review in our inspections as the total and showing the number that resulted in a comment form deficiency as a percentage.

Figure 19 – Nature of ICFR Auditing Deficiencies

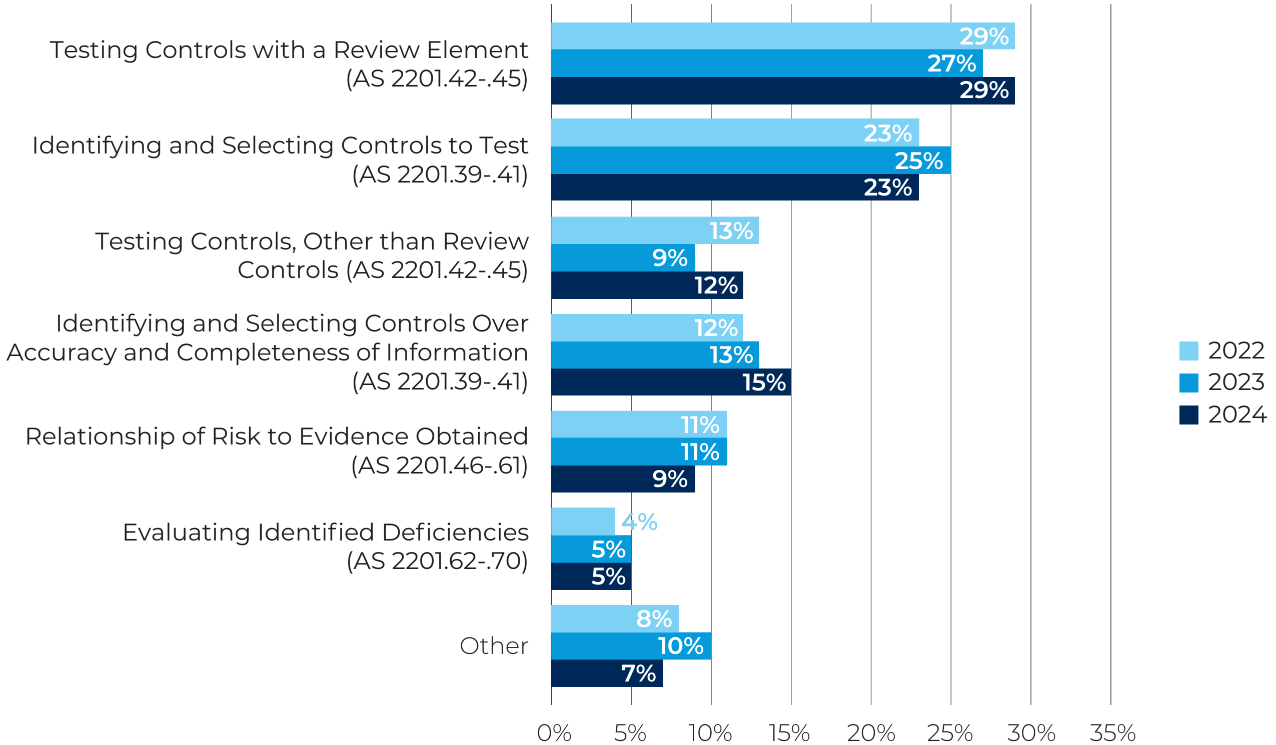
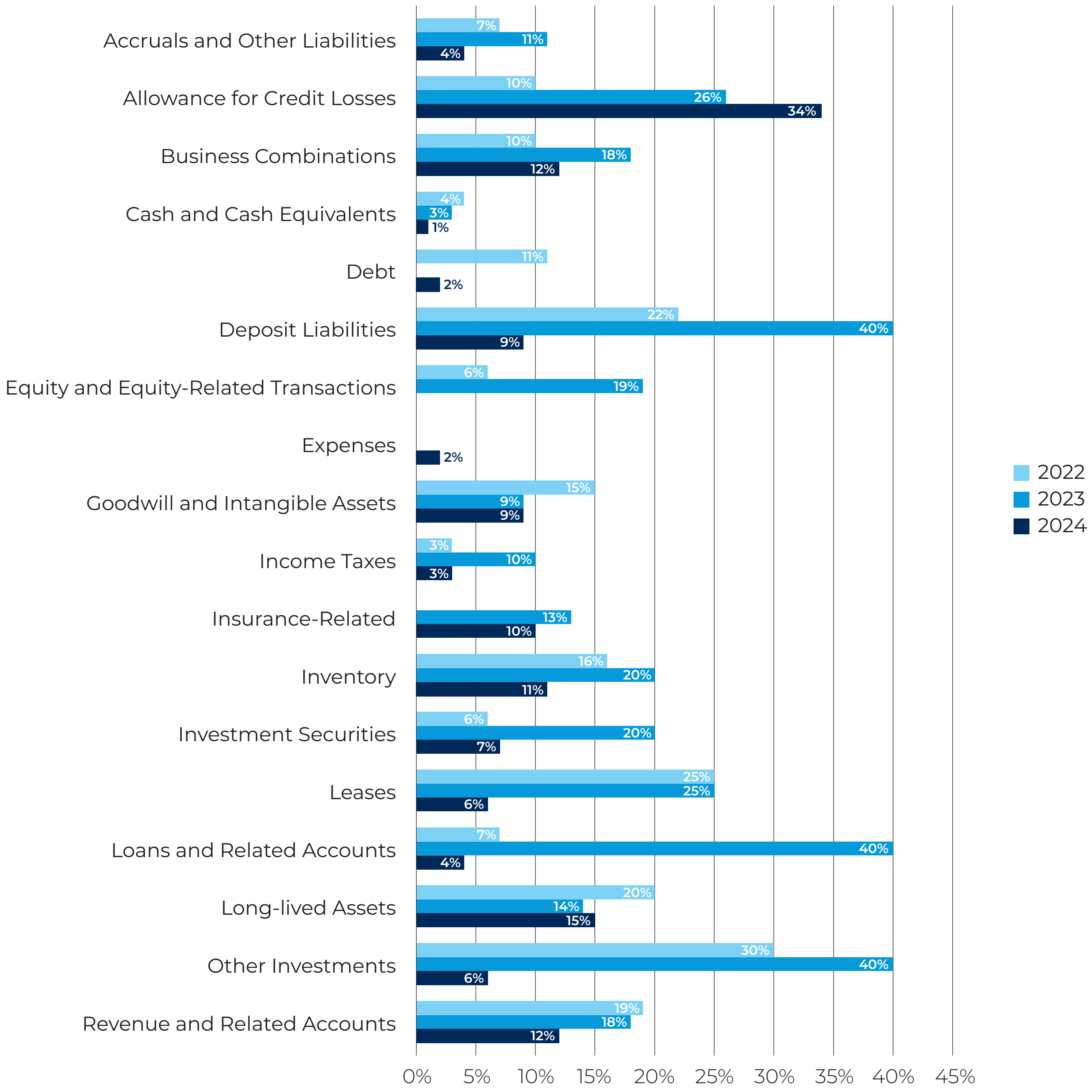


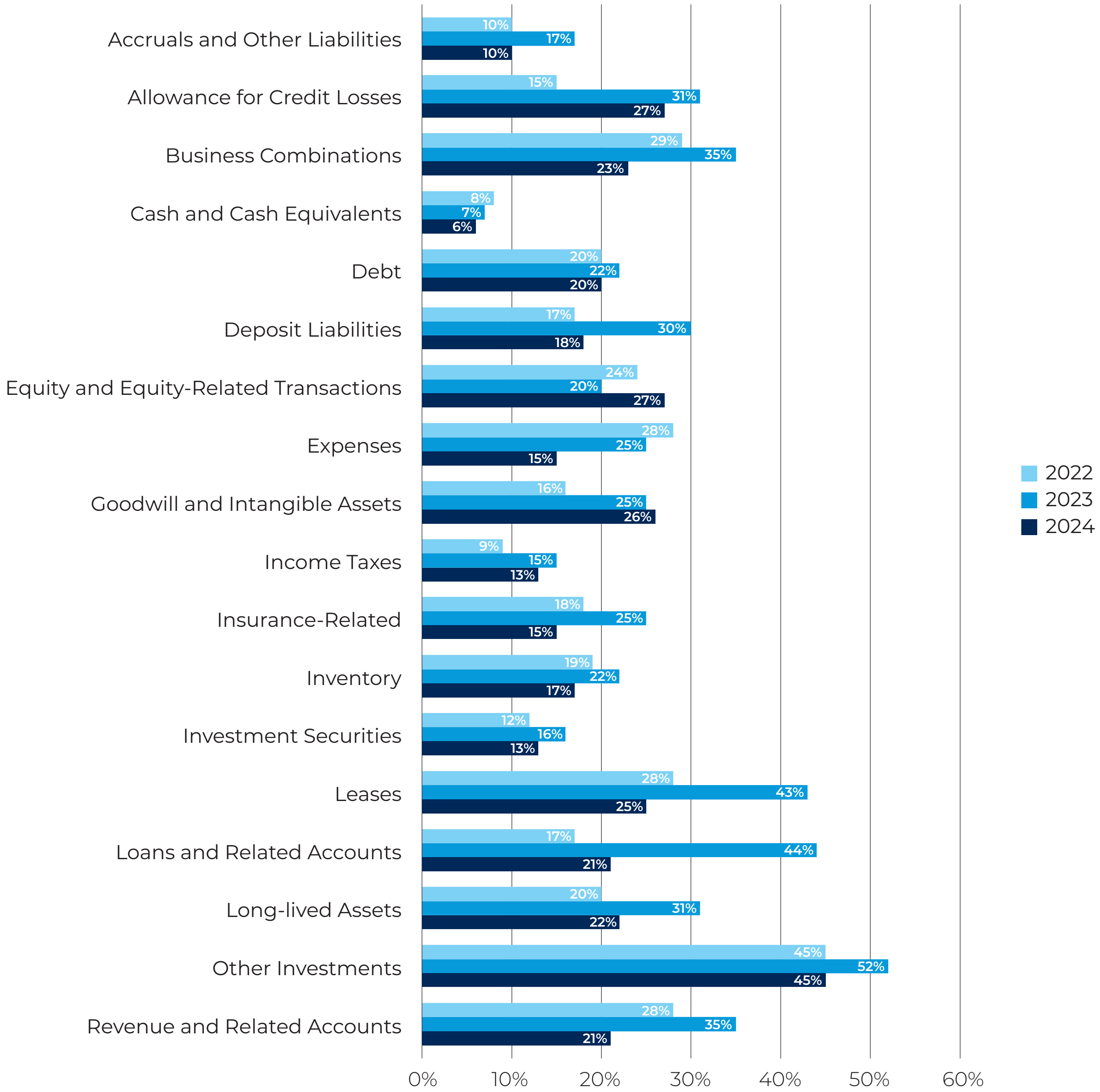
Figure 20 – Deficiencies in Auditing ICFR by Financial Statement Area



Deficiencies in Financial Statement Audit Areas

Financial statement areas that generated the most comment forms, excluding those that related to ICFR, can be seen in Figure 21.

Figure 21 – Common Financial Statement Deficiency Areas, Excluding ICFR



Tell Us What You Think

Was this Spotlight helpful to you? In fulfilling our mission to serve investors and the public, the PCAOB wants to know how we can improve our communication and provide information that is timely, relevant, and accessible. We welcome comments on this publication or other matters. You can fill out **our short reader survey** or email us at **info@pcaobus.org**.

APPENDIX: ABOUT PART I.A FINDINGS

Context: Issuer Financial Reporting Requirements

For an issuer to comply with SEC reporting requirements, the issuer must include with certain filings an independent auditor's unqualified opinion that the issuer is presenting certain financial information fairly, in all material respects, in conformity with the relevant accounting framework. In many cases, the filing must also include the auditor's opinion on whether the issuer maintained, in all material respects, effective ICFR.

To issue an unqualified opinion, PCAOB standards require that auditors must plan and perform audit procedures to obtain sufficient appropriate audit evidence that provides a reasonable basis for their audit opinions. The auditor's report (containing the opinion) must include a section captioned "Basis of Opinion." In that section, the auditor must represent that its opinion is based on an audit that the auditor conducted in accordance with PCAOB standards and must recite that those standards require the auditor to "plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud." An issuer's audit committee engages a registered public accounting firm to plan and perform such an audit sufficiently for the firm to obtain the reasonable assurance necessary to support the audit opinion to meet its reporting requirements.

PCAOB Inspection Reviews of Selected Audits

A PCAOB inspection of a registered firm includes a review of selected aspects of some of the firm's audits. Inspectors' review of an audit occurs after the firm's audit opinion has been issued and included in an issuer's filing. In many of the reviewed audits, PCAOB inspectors do not identify any respect in which the selected aspects of the audit fell short of the requirements of PCAOB standards to a degree that calls into question the sufficiency of the audit evidence obtained to support the firm's opinion.

In other reviewed audits, however, PCAOB inspectors identify respects in which the firm's work fell short of the requirements of PCAOB standards to such a degree that the firm appears not to have obtained sufficient appropriate audit evidence to support its opinion. Consequently, in those audits, the auditor did not "plan and perform the audit" sufficiently to satisfy its fundamental responsibility to "obtain reasonable assurance" about whether the financial statements are free of material misstatement, whether due to error or fraud.

Such an inspection finding does not necessarily mean that the financial statements are materially misstated (or that ICFR is ineffective). But it does reflect a conclusion that, at the time the audit opinion was issued and included in the issuer's filing, it could not be relied upon as providing reasonable assurance that the financial statements are free of material misstatement, whether due to error or fraud (or that ICFR is effective). In response to such a finding, firms often perform additional work. This work may confirm the validity of the original opinion or, in some cases, leads to the discovery of a material misstatement or material weakness that the firm had not detected before issuing its earlier opinion, and those discoveries have led issuers to restate financial statements and the auditor to reissue its opinion.[11]

Part I.A of a PCAOB Inspection Report

Part I.A of a PCAOB inspection report is dedicated exclusively to discussion of circumstances, as described above, in which the firm issued an audit report expressing an audit opinion without having obtained sufficient appropriate audit evidence to support that opinion. Part I.A discusses each such audit separately, and within the discussion of each such audit describes the auditing deficiency (or, in some audits, multiple deficiencies) that form the basis of the conclusion that the firm did not plan and perform the audit sufficiently to obtain reasonable assurance about the matter opined on (the financial statements and/or ICFR).[12]

> Because a Part I.A. deficiency means the audit firm failed to obtain sufficient appropriate evidence to support its opinion, and that an audit opinion was signed without completing the audit work required to verify the accuracy of the financial statements, it is paramount that firms work toward continual improvement.

[11] In the typical case, information available to inspectors in relation to a firm's deficient auditing is not sufficient for inspectors to form a judgment about whether there is an undetected material misstatement (or material weakness in ICFR), and that question can only be resolved through the auditor's performance of additional work. On occasion, however, information available to inspectors is sufficient to indicate that there appears to be a material misstatement (or material weakness in ICFR) that the auditor failed to identify and appropriately address (such as, for example, by withholding an unqualified opinion unless the issuer corrected the misstatement).

[12] For additional discussion concerning Part I.A findings, see the Board's description of related points in Information for Audit Committees about the PCAOB Inspection Process, PCAOB Release No. 2012-003 (August 1, 2012) at 3-7, A-1 – A-3 (note that, at the time of the 2012 Release, public inspection reports discussed only findings that are today reported in Part I.A, so where the Release's references to the "public portion of an inspection report" correspond to what is now referred to as Part I.A of an inspection report).