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Via email: comments@pcaobus.org

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 055

Dear Office of the Secretary:

We are pleased to provide comments to the Board and Staff on the April 9, 2024 Release No. 2024-003, *Firm Reporting* (the "Proposal"). In a separate letter, we also respond to Release No. 2024-002, *Firm and Engagement Metrics* (Docket Matter No. 041). While we have issued separate letters to these two proposals, some of our responses share some common themes.

Baker Tilly US, LLP ("Baker Tilly," "we," or "our") currently audits under 100 issuers, very few of which are accelerated or large accelerated filers ("AFs" and "LAFs", respectively). Although we are a top-10 ranked firm, our organization is in the PCAOB's category of a non-affiliated firm ("NAF"), which is substantially different from a Global Network Firm ("GNF").

General Comments on the Proposal

We recognize and appreciate the Board's goal of providing decision-useful information to investors and audit committees. However, there are several areas in which the Proposal falls short of that goal as well as several practical challenges to implementation. These concerns generally fall into the following categories:

- *Relevance or usefulness to stakeholder decision making* – certain of the new requirements do not appear to meet a threshold criterion of being relevant or useful to investors or audit committees. We believe investors' fundamental decision-making is based on issuer financial performance, not information about the firms that audit those issuers. It is the audit committee's statutory responsibility to represent the needs of investors and make informed decisions about the appointment and retention of auditors. Thus, it is far from clear that increased public disclosure by audit firms will lead to different investor decision-making. We do believe there is room for more dialogue between auditors and audit committees, but the topics to be addressed will vary from issuer to issuer, and private dialogue is a more productive path than a host of new public reporting requirements that may not be utilized by audit committees or investors, or confidential reporting that is used only by the PCAOB. Additionally, we believe some of the requirements are duplicative of other new PCAOB rules and standards or information the PCAOB already gathers in its inspection process.

- *Cost in proportion to potential benefit* – the benefits of some new requirements are unclear or hypothetical, and the Proposal's economic analysis does not attempt to quantify the related costs. As noted above, we do not believe several of the requirements will ultimately provide benefits to stakeholders at all, and other purported benefits are not sufficient to justify the related costs. Throughout the Proposal, there is a presumption that more disclosure is generally beneficial, but this presumption is unsubstantiated. The concept of costs is largely disregarded, raising questions as to how the SEC could approve a final rule without a robust cost-benefit analysis. Direct costs would include implementation of new processes and procedures to collect and produce the required information by audit firms, likely resulting in higher audit fees for investors. Indirect costs would include opportunity costs as firms redirect scarce resources to satisfying these new reporting requirements, which could be better used by allocating those resources to audit execution or quality control remediation and/or monitoring efforts.[1] On balance, we do not believe the benefits will outweigh the costs for several of the new requirements.

- *Information outside the Board's oversight authority* – it is difficult for firms to comment on legal matters, but several new requirements seem to require public production of information that is confidential or otherwise outside of or unnecessary for the Board's oversight function. Additional complexities related to confidentiality may exist for non-U.S. registered firms and the applicability of PCAOB Rule 2207.

- *Unclear or subjective terminology* – the Proposal contains a mix of principles- and rules-based reporting requirements. Particularly for requirements that require a materiality determination or those that use language requiring the exercise of judgment as to what should be reported, we urge the Board to embrace the spirit of principles-based requirements and not use disagreements about firms' good faith judgments as a basis for increasing enforcement cases.

- *Timing challenges* – if the Proposal is issued in its current form, we believe additional time will be necessary for firms to comply, particularly given new quality control standards now pending SEC approval. We also believe it will be necessary and appropriate to include a pilot reporting period in a test environment – particularly for confidential information – prior to the final effective date to ensure a smooth transition.

We explain these and other comments on the Proposal in more detail in the accompanying appendix.

Conclusion

Finally, we reiterate concerns raised in prior comment letters regarding the pace and scope of the Board's standard setting agenda, the cumulative impact of all standard setting projects and changes, the impact to the audit profession and individual auditors, and the related costs to firms, individual auditors, issuers, and investors. We strongly encourage the Board to consider pausing or significantly slowing the pace of standard setting to allow the audit profession to focus on the implementation of other new standards and enable thoughtful post-implementation review of recently issued standards. For example, while the comment period for

[1] This point was reiterated by Board Member Ho on May 28, 2024 in her remarks at U.S. Chamber of Commerce - U.S. Public Company Audits: A Rapidly Changing Landscape. "It is one thing for a large firm to comply with the proposal's new reporting requirements as they are generally well staffed, but for smaller firms facing challenges as a result of the "accounting talent crisis" and tight audit deadlines, the proposal's additional reporting requirements would re-direct scarce professional staff time away from performing audits to satisfying additional PCAOB reporting requirements that have no clear connection to audit quality. To put it another way, the PCAOB's proposal carries with it opportunity costs that could end up hurting audit quality and the investors we are sworn to protect by forcing firms to spend more time reporting and less time auditing. The burdens could also cause smaller firms to exit the public company audit marketplace resulting in less competition and higher audit fees that are ultimately borne by investors."

this Proposal was open, the Board voted to approve new standards on firms' systems of quality control and general responsibilities of the auditor.[2] The new quality control standard in particular will be a significant implementation undertaking, and imposing additional reporting requirements during the implementation period only increases the burden on an already strained audit profession. Particularly when the benefits are so unclear and the costs are unquantified, we caution the Board that proceeding at this pace may yield unintended consequences.

As Board Member Ho noted in her dissent on this Proposal:

> I am profoundly worried that the Board's apparent zeal to impose, in each new proposed standard or rule, new burdens on firms, without sufficient tailoring and without quantifying the estimated burdens, may end up breaking the public company auditing profession's back, particularly for small firms. If we "break" the profession in the name of investor protection, are we really protecting investors?[3]

We also echo the concerns raised by the Center for Audit Quality ("CAQ") in its May 22, 2024 comment letter[4] regarding the short comment periods for this and other proposals and the inability of firms to fully evaluate the hundreds of pages of proposal content and provide thoughtful comments to the Board and staff. The same day of the CAQ's letter, PCAOB Chair Williams spoke virtually at the PCAOB's *Forum on Auditing in the Small Business Environment and on Auditing Broker-Dealers* in Chicago, Illinois. In her remarks, Chair Williams made the following points:

> "Last year the Board took more formal actions on standard setting and rulemaking than any year since 2013. That work continues in 2024. So far this year, we've issued three proposals to modernize, clarify, streamline, and strengthen our rules and standards. We've also adopted new standards and amendments through two projects that have been informed by robust input from a wide variety of stakeholders, including small firms."
>
> "Once we've proposed a new or amended standard or rule, we look for more perspective through the public comment process. We encourage small firms to give us their unique perspectives.
>
> This input is incredibly valuable for us, and it shows up in our rules and standards."

These points simultaneously acknowledge the rapid pace of standard setting while emphasizing the value of stakeholder input, including from smaller firms. A 60-day comment period amid multiple other open proposals and newly issued final rules, at times during peak audit busy season, is simply not sustainable or practical for smaller firms to provide the meaningful input the Board claims it values.

We thank you for the opportunity to present our views on the Proposal and appreciate your consideration. We would be pleased to discuss these comments further with you.

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[2] PCAOB Release Nos. 2024-004 and 2024-005, May 13, 2024.
[3] Statement of Board Member Ho, April 9, 2024.
[4] This letter has been posted to PCAOB Rulemaking Dockets 041 and 055.

Sincerely,

Baker Tilly US, LLP

BAKER TILLY US, LLP

APPENDIX – RESPONSES TO CERTAIN ASPECTS OF THE PROPOSAL

A. FINANCIAL INFORMATION

1. Fee Information

The Proposal would amend Form 2 to require registered firms to report actual dollar amounts. The Proposal states that:

> Reporting in actual dollar amounts would allow stakeholders to better compare audit practice size from firm to firm, which the current percentage figures do not facilitate. This may help investors, audit committees, and other stakeholders better compare the extent of firm resources.[5]

This requirement is tantamount to providing a detailed segment disclosure of actual revenue across each of a firm's service lines. This requirement contradicts the confidential treatment of firm financial statements discussed in the following section and we believe such disclosure is entirely unnecessary for informed decision-making by any stakeholder. It also exceeds the scope of the Board's authority to mandate public disclosure of fee information for services outside the PCAOB's jurisdiction. Dollar amounts should remain confidential proprietary information.

We believe that the current percentage disclosures in Form 2 are more than adequate to understand the extent to which a firm focuses on public company audits. This is particularly true for smaller firms. However, if the Board believes a bit more disaggregation is warranted, we would support expanding the current percentage disclosures in Form 2 Item 3.2 to include broker-dealers and the proportion of audit and non-audit services for issuers and broker-dealers compared to the entire firm.

Finally, regardless of the approach the Board adopts, we believe clarification will be necessary for registered firms with alternative practice structures.

2. Financial Statements

We believe this new requirement is fraught with problems.

- This requirement is well beyond the Board's oversight authority. The PCAOB's jurisdiction plainly does not extend to financial information related to service lines that have nothing to do with public company audits.
- Full financial statements of the firm's entire operations are not necessary to understand a firm's practice or its overall financial stability. It is very unclear how the Board intends to use this highly confidential and sensitive financial information, and more justification is

[5] Proposal, pages 24-25.

necessary beyond the assertion that it would "enhance the PCAOB's oversight and monitoring of these firms and the audit market."[6]

- The Board does not have authority to mandate that firms adopt a particular financial reporting framework. For most firms subject to this proposed requirement, we believe the conversion costs will be massive, with little or no net benefit. These new financial statements are unlikely to be utilized by any party but the PCAOB, making this requirement unduly burdensome and costly. If the Board proceeds with a requirement for large firms to provide financial statements, we believe it can accomplish its objective by receiving whatever form a firm's financial reporting currently takes, as this is the form the firm uses to manage its operations and may be the required form under partnership agreements or bank covenants. If the PCAOB has questions, it can ask as part of the inspection process, given the firms that would be subject to this requirement are all annually inspected.
- We also believe it would be entirely inappropriate and outside the Board's authority to require public disclosure of this information.
- This requirement introduces yet another threshold, this time for firms who issued over 200 reports and have more than 1,000 personnel. Other than the proportion of market capitalization referenced in footnote 63 of the Proposal, it is unclear how this threshold was determined. We fear this requirement will serve as yet another disincentive for smaller firms to expand their public company audit practices and encourage the Board to consider a higher threshold such as 500 reports. We do not believe the number of personnel is as relevant to this threshold as the number of issuer audit reports a firm issues.

B. GOVERNANCE INFORMATION

Certain aspects of this proposed requirement are duplicative with the requirements of Form QC and Rule 2203A, which were adopted by the Board on May 13, 2024,[7] and should be removed from this Proposal. These include, without limitation:

- The individuals responsible for various components of the QC system
- The governing board or management committees
- The executive officer(s) who oversee(s) the firm's audit practice
- The external quality control function

We also believe several aspects of this requirement are not necessary or helpful for the Board's oversight or stakeholder decision making. For example:

- *All direct reports of the principal executive officer including names and titles*

  It is unclear what purpose this serves if some of the direct reports have no involvement in the audit practice or quality control.

- *Description of the legal structure, ownership, and governance of the firm*

[6] Proposal, page 26.
[7] PCAOB Release No. 2024-005.

The PCAOB already obtains partnership agreements and other governance information as part of the inspection process. We do not believe public disclosure of firms' governance structures is necessary for stakeholder decision making. Additionally, ownership – particularly percentages – is confidential information and should not be disclosed publicly.

C. NETWORK INFORMATION

Firm network structures can vary widely, and the networks of many smaller firms are not a significant factor in those firms' provision of audit services to issuer or broker-dealer clients. Consequently, we believe this requirement should apply only to larger firms that perform a significant number of multinational audit engagements.

However, even if the threshold is changed, we are unclear what purpose this information serves. The PCAOB already receives information about firms' networks in the inspection process, and it is unclear how public disclosure of that information would impact stakeholder decision-making. We are also concerned about users' understanding of firm networks; networks that share the same branding or name are often comprised of independently owned and operated firms. We believe this information is likely to be misused or misinterpreted.

Additionally, some of the information requested in the proposed requirements is confidential or sensitive. We do not believe it is appropriate to require public disclosure of network financial arrangements or legal structures, as registered firms are not necessarily permitted to share this information publicly. In the case of our firm, the network itself is not a registered firm, and many network members are similarly not registered. Requiring a registered firm to disclose operating principles of non-registered entities appears to be beyond the scope of the PCAOB's authority.

If the Board proceeds with this requirement, we believe more explanation will be required in a final rule. For example, it is not clear what is meant by the word "accountable" in Item 5.2.b's requirement to disclose "network governing boards or individuals to which the registered entity may be accountable." We recommend a more principles-based approach to this disclosure similar to the current Form 2 requirements.

D. SPECIAL REPORTING

We have several concerns about this section of the Proposal and have attempted to organize them by category.

1. Timing Requirements and General Comments

We have two primary concerns and recommendations for clarification regarding the new timing requirements:

- First, we question why a change from 30 to 14 days for Form 3 reporting is necessary or what the PCAOB will do differently by receiving the required information 16 days earlier. Many Form 3 events are routine changes for which expedited reporting does not appear necessary.

- Second, it is unclear what "or more promptly as warranted" is intended to mean and how the PCAOB intends to enforce this phrase. If the requirement is 14 days, the rule should state 14 days; it should not introduce subjectivity as to when reporting is required. The example cited on Page 38 seems to imply a shorter timeframe will be expected in certain circumstances, without explanation of exactly how quickly the Board expects firms to file a Form 3. We believe Board rules must be capable of objective measurement, and compliance requirements should be clear and precise. As one example, we do not believe the Form 3 reporting timeframe should be expedited simply because a matter has been reported in the press. While firms often file Forms 3 earlier than the current required timeframe, the rule itself should not contain subjective language as to when such filings are required.

2. Triggering Events

We question the Proposal's explanation of triggering events. We do not believe it will be appropriate or even practical to file a Form 3 for anticipated future events; instead, we believe Form 3 requirements should be limited to events that have actually occurred. For example, page 38 of the Proposal discusses the preparation of public relations plans as an indicator that there is a substantial likelihood that an event will occur. We disagree with this assumption, as events can change significantly between the commencement of communication plans and the execution of a definitive agreement. Additionally, significant events, even though reasonably likely to occur, may not even be known to the people responsible for filing Form 3 until communication plans are finalized. For example, in both of the following cases, we do not believe these events should be required to be reported until there is a definitive agreement and an anticipated effective date.

- *Planned or anticipated acquisition of the firm, change in control, or restructuring, including external investment and planned acquisition or disposition of assets or of an interest in an associated entity*

  In addition to concerns about the timing of this disclosure, we believe a materiality consideration is necessary. In some cases, a planned acquisition or disposition may not be material to a firm, and firms should not be required to disclose every transaction if a given transaction has no effect on the firm's public company or broker-dealer audit practice, and thus is not subject to the PCAOB's oversight.

- *That the firm has entered into, or plans to enter into, a definitive agreement or other arrangement that would cause a material change to the firm's operations or provision of services (e.g., spinning off a consulting business or severing a portion of the business for private equity involvement)*

  Again, we believe the triggering event for the disclosure should be the execution of a definitive agreement, not "plans to enter into" such an agreement.

3. *Confidentiality*

Page 6 of the Proposal states the expanded special reporting requirements would be on a confidential basis. However, the discussion of the new requirements on pages 34-39 contains only one reference to confidentiality.[8] Additionally, the text of the rule amendments in Appendix I contain only a request for confidentiality, so it is not abundantly clear whether all new special reporting requirements will be afforded confidential treatment. Accordingly, we recommend incorporating this into any final rule.

We also question the Board's authority to request disclosure (confidential or not) of aspects of a firm's operations that have no relevance to its auditing of issuers or broker-dealers.

4. *Scope of Reporting Requirements*

We believe Part VIII of Form 3 requires clarification as we are aware that several readers have interpreted the language differently. The threshold question is whether the event or matter "poses a material risk, or represents a material change, to the firm's organization, operations, or provision of audit services."[9] It goes on to state that, "[s]uch events or matters would include, but would not be limited to…" the list of items in Item 8.1. It is unclear whether the phrase "would include" represents a presumption that all items in this list that do not contain the word "material" are automatically required.

We are also concerned that the list of new reporting requirements is not exhaustive. Like our comments on the timing requirements above, given the Board's current stance on Form 3 enforcement, we believe any new reporting requirements should be explicitly clear in the text of any final rules, and not contain subjective language like "would not be limited to…"

5. *Materiality*

Footnote 85 on page 35 of the Proposal provides an illustrative example regarding a solvency-threatening change in revenue or a significant revenue increase necessitating significant staffing increases or other comparable organizational changes. While these are helpful illustrations, we believe the Board should be clearer in the materiality guidance on pages 37-38. We also believe materiality guidance should be embedded in the text of the final rule, not limited to the narrative discussion in the adopting release.

Some of the new required disclosures are incredibly subjective and vague, even with a materiality threshold. We recommend being clearer that qualitative materiality considerations may often be more relevant to this determination than quantitative ones. For example, firm revenue may change in ways that might be quantitatively material in an audit context, but such changes usually do not pose material risk, and, therefore, should not require Form 3 reporting.

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[8] Proposal, Page 36: "As discussed above, we propose that material events be reported confidentially."
[9] Proposal Appendix 1, Form 3, Item 8.1.

Additional concerns include:

- *Entering into or disposing of a material financial arrangement that would affect the firm's liquidity or financial resources (such as a line of credit, revolving credit facility, loan, or other financing), or group of related arrangements*

  In most cases, a routine financing arrangement will have no impact on a firm's audit practice so it is unclear how the materiality principle would be applied to these transactions. As noted above, we believe qualitative materiality will be much more relevant to a firm's reporting of this type of arrangement.

- *Material changes in the insurance or loss reserves of the firm and material changes related to captive insurance or reinsurance policies, including events that triggered material claims on such policies*

  We believe this requirement is well beyond the scope of the PCAOB's oversight authority. Unless such events fall within the scope of existing Form 3 reporting requirements, we do not believe this item should be included in a final rule.

- *Material changes in the amount of unfunded pension liabilities*

  In addition to the materiality considerations, this information is likewise well outside the PCAOB's oversight authority.

- *Any other planned or anticipated material amendments or changes to the firm's organization, legal structure, or governance*.

  Again, it is unclear how the materiality principle would be applied to these types of changes. For example, regarding governance structures, routine changes to board members would generally not be considered material, so we expect disclosures for this item would be limited to more significant changes to a firm's organization, legal structure, or governance.

6. *Implementation Costs*

Page 38 of the Proposal references "greater automation in the reporting function at some firms." We are unclear what automation the Board believes will expedite or reduce compliance costs of these broad new requirements. We believe the list on page 35 will require a significant amount of manual coordination among people in several different functions within a firm other than the quality control function (e.g., legal, finance, c-suite, operations). Consequently, we believe the Proposal significantly underestimates the complexity and cost of this significant expansion of reporting requirements, particularly given the shorter reporting timeframe proposed.

E. CYBERSECURITY

1. *Cybersecurity Incident Reporting*

We have several concerns and recommendations for clarification regarding the new cybersecurity incident reporting requirements:

- *Scope* – While we support timely confidential disclosure of cybersecurity incidents, we believe the scope of this requirement should be limited to events that have affected a firm's issuer or broker-dealer audit practices and are thus relevant to the PCAOB's oversight. While portions of the Proposal appear limited only to events relevant to the PCAOB's oversight,[10] the text of this proposed rule is broader.

- *Growing inconsistency* – We are concerned that cybersecurity professionals will become confused by the growing number of different and inconsistent cybersecurity reporting regulations and frameworks. The Proposal uses language different from the SEC's cybersecurity reporting rules, so we recommend considering the risks of introducing yet another reporting framework. Proposed Form 3 Item 9.1 also uses several subjective terms. Similar to our discussion regarding materiality above, we encourage the Board to respect good-faith judgments of firms in making these determinations and not use disagreements about those judgments as a basis for increasing enforcement cases.

- *Information to be reported* – Page 40 of the proposal states "We would expect such confidential reports to include sufficient information for the PCAOB to understand…" followed by a list of example disclosures. However, the text of Form 3 Item 9.1 in the Proposal's Appendix, simply requires a box to be checked followed by a "brief description of the event." If the Board proceeds with this requirement, we believe expectations as to what information should be included in the reporting should be written into the text of the rule and within Form 3's instructions, not limited to commentary in an adopting release.

- *Timing* – Finally, we reiterate the timing concerns described in section D.1 above. In this case, the reporting period is measured from the time the firm determined the event to be significant. We believe reporting within 30 days is still sufficient to meet the Board's objective, and a longer timeframe would also enable firms to provide more substantive information.

2. *Cybersecurity Policies and Procedures*

Our primary concern with the proposed Form 2 requirement to disclose cybersecurity policies and procedures relates to the usefulness of the information. The Proposal states the reporting, "…is not intended to elicit detailed, sensitive information but rather to inform the PCAOB, investors, audit

[10] *See, e.g.*, Proposal page 40: "Confidential reporting of significant cybersecurity incident information is important to the Board's ability to understand significant events at the firms it oversees and to assess whether their operations and/or issuer and investor information has been compromised in a way that would affect the provision of audit services or that otherwise merits follow-up."

committees, and other stakeholders of the firm's general policies and procedures, if any, to identify and manage cybersecurity risks."[11] This language makes clear the fact that the Board understands that disclosing sensitive details of cybersecurity policies and procedures is extremely unwise; consequently, we question the usefulness of this disclosure to stakeholders if it is of a general nature. The necessity of this information is also reduced by the fact that more detailed information is part of the PCAOB's inspection requests and is often discussed with audit committees or issuer management. We do not believe disclosing "general policies and procedures" will be helpful to any stakeholder given how guarded the disclosures will be.

F. UPDATED DESCRIPTION OF QC POLICIES AND PROCEDURES

Our primary concern with this requirement is for registered firms that are not currently providing audit services to issuers or broker-dealers. We do not believe this requirement should be triggered until those firms' circumstances change and they become actively engaged in the provision of audit services for entities subject to the PCAOB's oversight.

[11] Proposal, page 41.