

Via Email

August 1, 2024

Ms. Phoebe W. Brown
Office of Secretary
Public Company Accounting Oversight Board
1616 K Street, NW
Washington, DC 20006-2803

PCAOB Rulemaking Docket Matter No. 056, Proposed Auditing Standard – Designing and Performing Substantive Analytical Procedures and Amendments to Other PCAOB Standards.

Dear Secretary Brown:

The Council of Institutional Investors (CII) appreciates the opportunity to share our views and provide input on the Public Company Accounting Oversight Board’s (PCAOB or Board) *Proposed Auditing Standard – Designing and Performing Substantive Analytical Procedures and Amendments to Other PCAOB Standards* (Proposal).¹ CII supports the Proposal.

CII is a nonprofit, nonpartisan association of U.S. public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of approximately \$4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families, including public pension funds with more than 15 million participants – true “Main Street” investors through their pension funds. Our associate members include non-U.S. asset owners with about \$4 trillion in assets, and a range of asset managers with more than \$40 trillion in assets under management.²

CII Policies

As the leading U.S. voice for effective corporate governance and strong shareholder rights, CII believes that accurate and reliable audited financial statements are critical to investors in making informed decisions, and vital to the overall well-being of our capital markets.³ That belief is

¹ See Proposed Auditing Standard – Designing and Performing Substantive Analytical Procedures and Amendments to Other PCAOB Standards, PCAOB Release No. 2024-006 (June 12, 2024), <https://assets.pcaobus.org/pcaob-dev/docs/default-source/rulemaking/docket-056/2024-006-as-2305-proposal.pdf>.

² For more information about the Council of Institutional Investors (“CII”), including its board and members, please visit CII’s website at <http://www.cii.org>.

³ See CII, Policies on Other Issues, Independence of Accounting and Auditing Standard Setters (updated Mar. 1, 2017), http://www.cii.org/policies_other_issues#indep_acct_audit_standards.

reflected in the following CII membership-approved policy on the **Independence of Accounting and Auditing Standard Setters**:

Audited financial statements including related disclosures are a critical source of information to institutional investors making investment decisions. The efficiency of global markets—and the well-being of the investors who entrust their financial present and future to those markets—depends, in significant part, on the quality, comparability and reliability of the information provided by audited financial statements and disclosures. The quality, comparability and reliability of that information, in turn, depends directly on the quality of the . . . standards that . . . auditors use in providing assurance that the preparers’ recognition, measurement and disclosures are free of material misstatements or omissions.⁴

Our policy on **Independence of Accounting and Auditing Standard Standards** also states that CII “has consistently supported the view that the responsibility to promulgate . . . auditing standards should reside with independent organizations.”⁵ And that the “attributes that underpin an effective . . . auditing standard setter include:

- **Independence and Technical Expertise** – A full-time standard-setting board and staff that are independent from prior employers or similar conflicts and possess the technical expertise necessary to fulfill their important roles;
- **Accountability to Investors** – A clear recognition that investors are the key customer of audited financial reports and, therefore, the primary role of audited financial reports should be to satisfy in a timely manner investors’ information needs (this includes having significant, prominent and adequately balanced representation from qualified investors on the standard setter’s staff, standard-setting board, oversight board and outside monitoring or advisory groups);
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- **Enforcement** – A clear, rigorous and consistent mechanism for enforcement by regulators of the . . . auditing standards.”⁶

Our membership-approved policy on **Auditor Independence** includes the following language that we believe may also be relevant to issues raised by the Proposal:

The audit committee should fully exercise its authority to hire, compensate, oversee and, if necessary, terminate the company’s independent auditor. In doing so, the committee should take proactive steps to promote auditor independence and audit quality.⁷

⁴ *Id.*

⁵ *Id.*

⁶ *Id.*

⁷ CII, Policies on Corporate Governance, § 2.13a Audit Committee Responsibilities Regarding Independent Auditors (last updated Mar. 6, 2023), https://www.cii.org/corp_gov_policies.

Finally, CII also has a long-standing, membership-approved policy on **Financial Gatekeepers**.⁸ That policy explicitly identifies external auditors as financial gatekeepers.⁹ The policy indicates that it is imperative that auditors be subject to “[r]obust oversight and [have] genuine accountability to investors. . . .”¹⁰ The policy also states that “[c]ontinued reforms are needed to ensure that the pillars of transparency, independence, oversight and accountability are solidly in place.”¹¹

The Proposal

At the outset we note that the Proposal would replace AS 2305, *Substantive Analytical Procedures* (Existing AS 2305)¹² “in its entirety.”¹³ We understand the Existing AS 2305 “was originally developed by the American Institute of Certified Public Accountants . . . [14], adopted on an interim basis by the Board in 2003, and remains in effect substantially as adopted.”¹⁵ Thus, we believe pursuing the implementation of the Proposal is a strong step forward toward achieving the *Board’s 2022-2026 Strategic Plan*¹⁶ and is directly responsive to the views expressed by CII in our related September 2022 letter to the PCAOB.¹⁷ In that letter we requested that the Board prioritize “as requested by [Securities and Exchange Commission] Chair Gensler, the Board’s standard setting project on ‘Interim Standards’”¹⁸ Our prioritization of the interim standards was based, in part, on our policy on the **Independence of Accounting and Auditing Standard Setters** that reflects the view that auditing standards

⁸ See CII, Policies on Other Issues, Financial Gatekeepers (adopted Apr. 13, 2010), https://www.cii.org/policies_other_issues#fin_gatekeepers.

⁹ See *id.* (“Auditors, financial analysts, credit rating agencies and other ‘financial gatekeepers’ play a vital role in ensuring the integrity and stability of the capital markets.”).

¹⁰ *Id.*

¹¹ *Id.*

¹² See AS 2305: Substantive Analytical Procedures (last visited July 9, 2024), <https://pcaobus.org/oversight/standards/auditing-standards/details/AS2305>.

¹³ PCAOB Release No. 2024-006 at 4.

¹⁴ We note that in 2012 the American Institute of Certified Public Accountants issued a standard that enhanced guidance on analytical procedures. See Analytical Procedures, AU-C Section 520 at 633 (Am. Inst. of Certified Pub. Accountants Dec. 15, 2012),

<https://us.aicpa.org/content/dam/aicpa/research/standards/auditattest/downloadabledocuments/au-c-00520.pdf>.

¹⁵ PCAOB Release No. 2024-006 at 4.

¹⁶ See Request for Comment, Draft 2022-2026 PCAOB Strategic Plan, PCAOB Release No. 2022-003 (Aug. 16, 2022), https://assets.pcaobus.org/pcaob-dev/docs/default-source/about/administration/documents/strategic_plans/2022-003-rfc-draftstrategicplan.pdf?sfvrsn=fdc9859a_4; PCAOB, Strategic Plan, 2022-2026, Draft for Comment 7 (Aug. 2022), https://assets.pcaobus.org/pcaob-dev/docs/default-source/about/administration/documents/strategic_plans/draft-2022-2026-strategic-plan.pdf?sfvrsn=65f830db_4 (“[A]s important as these standards are, some of them were written by the audit profession and have not been updated since before the PCAOB was established in 2003, when they were adopted on what was intended to be an interim basis [and] [t]he world has changed since 2003, and our standards must adapt to keep up with developments in auditing and the capital markets [and] [w]e intend to modernize and streamline our existing standards and to issue new standards where necessary to meet today’s needs.”).

¹⁷ See Letter from Jeffrey P. Mahoney, General Counsel, CII to Office of the Secretary, PCAOB 5 (Sept. 15, 2022), [https://www.cii.org/files/issues_and_advocacy/correspondence/2022/September%2015,%202022%20PCAOB%20letter%20\(final\).pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2022/September%2015,%202022%20PCAOB%20letter%20(final).pdf).

¹⁸ *Id.*

should be the product of an independent standard setting process that focuses on investors' needs.¹⁹

We also share PCAOB Chair Erica Y. Williams' view that Existing AS 2305 "does not reflect developments that have taken place in the auditing environment in the past 35 years, for example, advancements in technology and a greater availability of information that is being used by the auditing profession in obtaining audit evidence [and that] . . . there are certain requirements in the existing standard that are duplicative of other Board-issued standards, such as the requirements related to documentation."²⁰

We also support the Proposal because we believe, consistent with our policy on **Independence of Accounting and Auditing Standard Setters**, the proposed standard, if adopted, would institute more consistent and higher quality audit procedures, reducing variability in audit quality. And, as the Board has indicated, many auditors are already following some aspects of the proposed new requirements which may alleviate regulatory burdens.²¹

We also believe, consistent with our policy on **Independence of Accounting and Auditing Standard Setters**, that the Proposal would give the PCAOB's regulatory arm a more robust set of rules to better ensure that all auditors are delivering quality audits to investors. We are pleased that the inspection process informed these proposed new standards.²² Its involvement in the process suggests the Proposal is the result of an evidence based standard setting process.

¹⁹ See *id.* at 4 (referencing our policy on Independence of Accounting and Auditing Standard Setters in support for Securities and Exchange Commission Chair Gary Gensler's statement regarding the need for the Public Company Accounting Oversight Board to update the "interim standards").

²⁰ Erica Y. Williams, Chair, PCAOB, Chair Williams' Statement on Proposal To Replace Standard on Substantive Analytical Procedures (July 12, 2024), [https://assets.pcaobus.org/pcaob-dev/docs/default-source/rulemaking/docket-052/4_miag.pdf?sfvrsn=f77f0fec_4](https://pcaobus.org/news-events/speeches/speech-detail/chair-williams--statement-on-proposal-to-replace-standard-on-substantive-analytical-procedures#:~:text=Chair%20Williams%20Statement%20on%20Proposal%20To%20Replace%20Standard%20on%20Substantive%20Analytical%20Procedures,-Date%3A%20Jun.&text=Performing%20substantive%20analytical%20procedures%20is.a%20significant%20account%20or%20disclosure; see, e.g., Letter from Members of the Investor Advisory Group to the Office of the Secretary, PCAOB 1-2 (Aug. 25, 2023), <a href=) ("We agree with the Board's statement '...the use of information in electronic form and technology-based tools by companies and their auditors to analyze such information has expanded significantly since these standards were developed.'").

²¹ See PCAOB Release No. 2024-006 at 36 ("Some firms' methodologies already incorporate certain aspects of proposed AS 2305 . . .").

²² See *id.* at 10-13 (discussing: "Current Practice and Observations from PCAOB Oversight Activities"); Erica Y. Williams, Chair, PCAOB, Chair Williams' Statement on Proposal To Replace Standard on Substantive Analytical Procedures ("We observed through our oversight activities that auditors do not always design and perform substantive analytical procedures appropriately."); George R. Botic, Board Member, Statement in Support of Proposed AS 2305, Designing and Performing Substantive Analytical Procedures, and Amendments to Other PCAOB Standards (June 12, 2024), <https://pcaobus.org/news-events/speeches/speech-detail/statement-in-support-of-proposed-as-2305--designing-and-performing-substantive-analytical-procedures--and-amendments-to-other-pcaob-standards#:~:text=I%20am%20pleased%20to%20support,procedures%20to%20promote%20audit%20quality> ("It takes a standard that is over 30 years old, and has not been substantially changed since being adopted by the PCAOB in 2003, and considers it in light of the observations we have gathered in two decades of oversight activities."); Anthony C. Thompson, Board Member, PCAOB, Statement In Support of Substantive Analytical Procedures (June 12, 2024), <https://pcaobus.org/news-events/speeches/speech-detail/statement-in-support-of->

With the advancement in data analytic techniques, we see an excellent opportunity for technology to improve audit quality and reduce audit costs.²³ However, we have some concerns about the potential misuse of technology in a manner that reduces audit quality. We believe the additional guardrails around substantive analytical procedures contained in the Proposal could help to make technology advancements in auditing more beneficial to investors.

We appreciate the opportunity to provide CII's investor-focused perspective on the Proposal. Please let me know if you have any questions about the content of this letter.

Sincerely,

A handwritten signature in blue ink that reads "Jeff Mahoney". The signature is written in a cursive, flowing style.

Jeffrey P. Mahoney
General Counsel

[substantive-analytical-procedures](#) (“recent inspection results across all of our inspection programs indicate that there continue to be deficiencies in certain aspects of designing and executing substantive analytical procedures”).

²³ See, e.g., Letter from Members of the Investor Advisory Group to the Office of the Secretary, PCAOB at 4 (discussing how proposed technology-assisted audit procedures can lead to higher quality audits with benefits in excess of any related cost increases).