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By 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 No. 046: *PCAOB Release 2022-006: A Firm's System of Quality Control and Other Proposed Amendments to PCAOB Standards, Rules, and Forms*

Dear Office of the Secretary:

We appreciate the opportunity to comment on the Public Company Accounting Oversight Board's (PCAOB or the Board) Release No. 2022-006, *A Firm's System of Quality Control and Other Proposed Amendments to PCAOB Standards, Rules, and Forms* (Release). We would like to acknowledge the considerable effort and thoughtfulness that went into the creation of the Release, which includes the proposed integrated, risk-based standard, QC 1000, *A Firm's System of Quality Control* (QC 1000). We commend the Board for taking significant steps towards modernizing the existing PCAOB quality control (QC) standards. We recognize the importance and impact of this new QC standard on the capital markets and the profession given that an effective and robust QC system is foundational for audit quality. We strongly believe that a risk- and principle-based approach to quality control will protect investors while addressing the evolving landscape in which firms operate.

Consistency with other quality control standards

We appreciate the Board's careful consideration of other recently adopted QC standards during the development of QC 1000, including the International Standard on Quality Management 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements* (ISQM 1), adopted by the International Auditing and Assurance Standards Board (IAASB), and the Statement on Quality Management Standards No. 1, *A Firm's System of Quality Management* (SQMS 1), adopted by the AICPA (collectively referred to as the Other QC Standards herein). Building on a common, risk-based approach to quality control will contribute to more effective and efficient implementation efforts across firms of various sizes and complexities and significantly improve the quality of the resulting QC systems to support the consistent performance of audits and other engagements under PCAOB standards. As a member firm operating within a global network, we continue to believe that the ability to design, implement and operate a consistent and comprehensive system of quality control across a global network of firms will result in the highest level of audit quality with global consistency, which is important to relevant stakeholders.

At the same time, we also acknowledge that it is necessary for QC 1000 to appropriately reflect jurisdictional differences in the U.S. and other international regulatory and legal environments and serve to protect the needs and priorities of investors and the public interest. In consideration of the foregoing, we support commonality not only in the quality objectives of the QC standards, but also in the language used to describe the relevant requirements. For example, we discuss in the

appendix to this letter, our concerns with certain proposed terminologies that are different from the Other QC Standards, such as "QC deficiency" and "Major QC deficiency," which are likely to lead to diversity in practice of application and may ultimately undermine the expected benefits of the firm's enhanced QC system under QC 1000. Further, misalignment in the evaluation terminologies where a different evaluation conclusion could be reached for the same set of circumstances under QC 1000 versus the Other QC Standards could create risks and confusion for key stakeholders in the capital markets, such as audit committees and investors. Accordingly, we respectfully recommend the Board to further analyze the costs, benefits and potential unintended consequences associated with such differences and reconsider the possible alignment of certain terminologies in the final QC 1000 standard.

Evaluation and reporting of the firm's system of quality control

A critical aspect of the final QC standard will be the requirements to evaluate and report on the effectiveness of the firm's QC system. In that regard, we continue to support the position of allowing firms to choose their own annual evaluation date, instead of a specified evaluation date, as this will contribute to better alignment with timing of key operational activities that are an integral part of the firm's QC system and to avoid additional costs of performing two QC evaluations within the period of QC 1000 adoption, given that firms have already selected an annual evaluation date under ISQM 1, and like KPMG, we understand many other firms have selected dates other than November 30. We recognize the Board's consideration of aligning the evaluation date with firms' internal inspections process. However, we believe that firms' operational cycles as well as engagement performance should also be considered. We have highlighted specific operational challenges in the appendix associated with the proposed evaluation date of November 30 and would appreciate the Board's reconsideration in the final standard to allow for firms to select their annual evaluation date, which we believe best contributes to the quality of audits and the QC system.

In addition to our recommendation to align certain terminologies to the Other QC Standards, we also respectfully recommend the Board considers the retention and incorporation of the existing evaluation framework under Section 104(g)(2) of the Sarbanes-Oxley Act of 2002 (the Act). This framework focuses on substantial good faith progress made towards remediation instead of complete remediation, which is important to retain in the annual evaluation of the firms' effectiveness of their QC system to prevent potential confusion to capital market participants that will result when different information about a firm's QC system is reported by the firm and by the PCAOB in its inspection reports of the firm. This will also provide firms time to identify and implement relevant remedial actions in response to deficiencies, which will have the added benefit of providing the capital markets with more decision useful information than would be possible if firms are to report under the timeframes of the proposal. We believe this approach is also consistent with the continuous and iterative nature of a firm's QC system.

Relatedly, we have included several recommendations to modify the proposed communication requirements to audit committees under PCAOB AS 1301: *Communications with Audit Committees*. In particular, we are concerned the proposed requirements conflict with the current threshold and timing for when nonpublic QC information will be made publicly available under the framework of Section 104(g)(2) of the Act and it also may create confusion for audit committees because different information about a firm's QC system will be communicated by different parties (e.g., the PCAOB and the firm itself) at different times. As discussed in more detail in the

appendix to this letter, we have included a proposed solution for consideration, which anchors the reporting threshold to whether substantial good faith progress has been made towards remediation.

A principle-based approach to quality control

We support a principle-based QC standard that focuses on identifying the relevant quality objectives without specifying quality responses, as this principle-based approach enables firms to design and implement a QC system tailored to the unique risks and circumstances of the firm. Overly prescriptive requirements not only reduce the scalability of QC 1000 but may also negatively impact the quality and effectiveness of implementation as firms – to comply with specified quality responses – may need to implement policies and procedures to address quality risks that may not be relevant or the most effective for their circumstances. Specifically, we have shared some of our perspectives in the appendix on certain proposed specified quality responses that we suggest the Board reevaluate. We respectfully request the Board to reconsider the need to include incremental specified quality responses, particularly when allowing firms to identify quality risks and related responses applicable to their circumstances that can achieve the same or even higher levels of quality results against the quality objectives, as compared to the prescriptive quality responses in QC 1000.

Within this letter we have provided observations on these themes and have included in the appendix detailed responses to certain questions on which the Board requested feedback.

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We appreciate the Board's consideration of our comments and observations in support of revising the quality control standards to enhance audit quality, and we would be pleased to discuss our comments with the Board and its staff at your convenience. We look forward to continuing our engagement with the Board and its staff in support of our shared commitment of investor protection and audit quality.

Sincerely,

KPMG LLP

KPMG LLP

Appendix

Below are responses to select questions in the Release for which we had specific input.

Basic Structure, Terminology, and Scalability

5. Is it appropriate for the proposed standard to require firms that have not and do not plan to perform engagements pursuant to PCAOB standards to design a QC system in accordance with QC 1000? Why or why not? Would this requirement impose disproportionate costs on small firms? Please provide data or estimates, if available, on such costs.

We recommend the final QC 1000 standard allows firms that have not and do not plan to perform engagements pursuant to PCAOB standards the flexibility to choose to design a QC system in accordance with QC 1000 or one of the Other QC Standards such as ISQM 1. A requirement to design a QC system in accordance with QC 1000 for firms that have not and do not plan to perform engagements pursuant to PCAOB standards may not provide the firm or investors with a benefit that outweighs the cost of designing a QC system that may never be implemented and operated. In the Release, the Board acknowledges that, without engagements, implementation and operation of a QC system would be largely hypothetical and the associated risks to investor protection are minimal.

9. We intend the proposed standard to be scalable for all firms based on their nature and circumstances. Are there additional factors we should consider so that the proposed standard is scalable for all firms? If so, what are those factors? Should the standard be revised to make it more scalable? If so, how?

We support a scalable standard for all firms based on their nature and circumstances. We continue to believe it is important for QC 1000 to be principle-based, which will enable firms to determine the appropriate risks and responses relevant to the firm's size and complexity. We recommend the Board focus the final QC 1000 standard on identifying the required quality objectives while avoiding the use of specified quality responses as the prescriptive requirements of the specified quality response in the proposed QC 1000 can conflict with the objective of scalability. A standard without specified quality responses should achieve the same level of quality and enforceability as the proposed QC 1000 because firms will be required to design, implement, and operate QC systems to achieve the quality objectives. Such an approach will have the benefit of enabling firms to have flexibility to tailor their QC system to the specific quality risks that arise based on their specific circumstances and will allow them to increase quality by adapting and improving their responses for technological or other changes. We have provided specific suggestions regarding scalability in our responses to other questions below.

Roles and Responsibilities

12. Are the proposed requirements related to roles and responsibilities described in the standard clear and appropriate? If not, how should they be clarified or modified?

We recognize the importance of accountability and support the assignment of responsibility to individuals for the operational roles listed in paragraphs .11 and .12 of QC 1000. In addition to allowing firms to assign one individual to more than one of the roles identified in paragraphs .11 and .12, we believe that the final standard should allow firms to further break apart those four roles than what is described in QC 1000. This can be achieved by aligning with the firm's operational structure while still maintaining the concept that whether the firm assigns the responsibilities listed in paragraph .12 to four, five, six or any number of individuals, each of them

would have discrete responsibilities and a direct line of communication to the individual assigned with the ultimate responsibility and accountability for the QC system as a whole. This change would align with the scalability objective of QC 1000. The assignment of multiple individuals to one of the defined roles in QC 1000 would not diminish the responsibility of that role but would more efficiently and effectively operationalize accountability for the given role. For example, due to the various nuances related to ethics and independence, legal, and regulatory requirements, coupled with the volume of matters within such areas, firms may already have operating structures in place where the individuals with responsibility and accountability for ethics and independence differ. Requiring firms to assign the responsibility and oversight to only one individual for the combined ethics and independence role would necessitate operational and organizational structure changes that would increase the volume and scope of responsibility for a single individual and may result in unintended consequences. Specifically, our concern is one of reduced quality that may result from potential detraction in the depth of focus and competencies necessary to meet the overall scope of responsibility assigned to the role.

Additionally, we note that paragraph .12 of QC 1000 requires the assignment of relevant roles and responsibilities to “firm personnel,” which differs from the requirements under ISQM 1 paragraph .20, which does not specify that the individuals need to be "firm personnel." We support the importance of having individuals in these roles who (a) are accountable for the related responsibilities, (b) have the appropriate experience, knowledge, influence and authority within the firm, (c) sufficient time to fulfill their responsibilities, and (d) direct lines of communication to the individual assigned ultimate responsibility for the QC system. For some smaller member firms within a global network, the individuals fulfilling these roles may not always be ”firm personnel” as they may be from another member firm within the network with appropriately governed responsibilities within the smaller member firms. We believe the accountability and other important attributes for these individuals may be best achieved by not limiting the candidates for such to ”firm personnel.”

We recommend aligning paragraph .12 with the principle-based requirement in ISQM 1 by removing the explicit requirement for assignment to "firm personnel" and rely on the important principle-based requirements for these roles. This will provide the necessary flexibility to firms with differing legal and operational structures to implement a globally consistent QC system. We note that both QC 1000 and the Other QC Standards acknowledge the importance of the firm network structure and network activities (e.g., QC 1000 paragraph .66) and limiting the roles included in paragraph .12 to "firm personnel" is inconsistent with these principles.

The Firm’s Risk Assessment Process

16. Should the proposed definition of “quality risks” explicitly address risks of intentional misconduct by firm personnel and other participants? If not, please explain why. Should the definition explicitly address other risks? If so, what are the other risks?

We agree that it is appropriate for the definition of “quality risks” to explicitly include the risk of intentional misconduct. Recent enforcement actions by the PCAOB have highlighted the occurrence of a wide variety of misconduct across firms. We recognize that such misconduct can damage investor confidence. Therefore, we support the explicit requirement for firms to consider the risk of intentional misconduct by firm personnel and other participants.

17. In the proposed definition of "quality risks" should the threshold of "reasonable possibility of occurring" also apply to all risks, including risks of intentional misconduct by firm personnel and other participants? If so, why?

We believe that the threshold of "reasonable possibility of occurring" should apply to all quality risks, including risks of intentional misconduct. As defined, some may interpret the proposed definition of "quality risks" to require firms to consider, identify and evaluate *every* conceivable act of misconduct, which is inconsistent with the reasonable assurance objective of QC 1000 and contrary to certain commentary by the Board in the Release. For example, the Release states "[u]nder the proposed definition of quality risks, [...] limiting risks of intentional misconduct to only those that have a reasonable possibility of adversely affecting achievement of the firm's quality objectives would result in the firm concentrating its efforts on more pervasive and larger risks and not on every conceivable act of misconduct."

If the proposed definition is to expect firms to perform risk assessment procedures to identify every conceivable act of misconduct that could adversely affect the firm's achievement of one or more quality objectives, the quality risk would not be possible to mitigate because completeness of the population of possible acts of misconduct is not attainable. Further, this quality risk is also likely not possible to mitigate for other participants because it may require other participants to share information for which they are prohibited by law or regulation from sharing.

As such, we recommend the threshold of "reasonable possibility of occurring" apply to all risks, including risks of intentional misconduct. The "reasonable possibility" term in the proposed definition of "quality risks" is already aligned with the use of this term in other PCAOB standards and the Other QC Standards. We recommend that the same approach is retained in QC 1000 for risks of intentional misconduct. Such an approach would be analogous to PCAOB AS 2110: *Identifying and Assessing Risks of Material Misstatement*, which requires auditors to identify and assess risks of material misstatements, whether due to error or fraud.

Relatedly, PCAOB AS 2401: *Consideration of Fraud in a Financial Statement Audit* addresses management's responsibility to design and implement programs and controls to prevent, deter, and detect fraud. AS 2401 highlights the importance for management to set the right tone at the top, including a culture based on integrity and high ethical standards. The proposed quality objectives and specified quality responses in the Governance and Leadership and Ethics and Independence components of QC 1000 impose similar requirements for firms. Further, AS 2401 acknowledges that intent is often difficult to determine and that "although an audit is not designed to determine intent, the auditor has a responsibility to plan and perform the audit to obtain *reasonable assurance* about whether the financial statements are free of material misstatement, *whether the misstatement is intentional or not*." *[italics added for emphasis]* As such, removing the threshold of "reasonable possibility of occurring" for risks of intentional misconduct would result in imposing a threshold on firms that exceeds that of what current auditing standards impose on auditors to identify and assess risks due to fraud.

Based on the above, we believe the definition of "quality risks" could be clarified as follows:

> .A12 Quality risks – Risks that, individually or in combination with other risks, have a reasonable possibility of occurring and adversely affecting the firm's achievement of one or more quality objectives if the risks were to occur, including those arising from intentional misconduct or unintentional acts.

We respectfully encourage the Board to adopt the above proposed definition, which we believe could minimize the potential application inconsistency to the extent that some misinterpret the definition of "quality risks" as proposed in QC 1000.

Governance and Leadership

22. For the proposed specified quality response related to the firm's governance structure, is the threshold (firms that issued audit reports with respect to more than 100 issuers during the prior calendar year) appropriate? If not, what is an appropriate threshold?

We believe the proposed threshold is appropriate. However, we encourage the Board to consider explicitly including in the final standard the specified requirements to identify a cut-off date for firms to determine whether the threshold has been met (determination date) and provide a transition period for firms to action the corresponding specified quality response. We recommend that the Board defines a determination date of 12 months before the evaluation date, which will allow firms an appropriate time to implement the relevant requirements of the final standard after the threshold is met.

23. Is the proposed specified quality response to incorporate an oversight function for the audit practice for firms that issue auditor reports with respect to more than 100 issuers appropriate? If not, why not?

We believe the proposed specified quality response is appropriate. We encourage the Board to continue to be principle-based and thus allow for flexibility in how a firm establishes its oversight function.

Ethics and Independence

26. Are the proposed quality objectives for ethics and independence requirements appropriate? Are changes to the quality objectives necessary for this component? If so, what changes?

We agree that the proposed quality objectives for ethics and independence requirements are appropriate and important. We appreciate that the Release provides clarification regarding the ethics and independence requirements that apply to firm personnel and others. However, we believe that the quality objectives can be further clarified as it relates to the term "firm personnel." The proposed definition of "firm personnel" includes individuals assisting with "the design, implementation, or operation of the firm's QC system, including engagement quality reviews." As the term "firm personnel" is used throughout the quality objectives and specified quality responses in paragraphs .31 - .36 of QC 1000, it could be inferred that the ethics and independence requirements extend to all individuals involved in the operation of the firm's QC system, including those individuals who are not subject to the requirements under the existing PCAOB and SEC independence rules. For example, large firms will typically maintain large teams of employees to perform data research and other tasks supporting the firms' QC systems. Adding independence requirements for those individuals does not impact a firm's ability to maintain its independence in fact or appearance and may inhibit a firm's ability to attract and retain qualified employees for its QC system. We recommend the PCAOB clarify the term "firm personnel" in the ethics and independence quality objectives and specified quality responses of QC 1000 to explicitly refer to "firm personnel", who are subject to the ethics and independence requirements."

27. Are the proposed specified quality responses for ethics and independence requirements appropriate? If not, what changes to the specified quality responses are necessary for this component?

As discussed previously, we do not believe specified quality responses are necessary to achieve the objectives of the QC 1000 proposal. The specified quality responses, as drafted, are written in a prescriptive way that will quickly outdate the standard and require actions that may be done in more effective ways, now and in the future. Instead of including prescriptive specified quality responses, we recommend that the standard include more specified quality objectives. Including specified quality objectives will facilitate firms in identifying risks and developing appropriate responses, while promoting scalability and allowing for future adaptations to technological or other innovations. However, if the specified quality responses are required, we have the following specific comments.

- Paragraph .34c requires that the list of restricted entities be reviewed prior to the occurrence of certain activities. We recommend that firms be permitted to develop quality responses to identify prohibited relationships and fee arrangements that appropriately respond to quality risks, based on the firm's individual facts and circumstances, rather than requiring the specific quality response noted in the proposal.

- Paragraph .34d(2) of QC 1000 requires firm personnel to review the list of restricted entities when changes to the restricted entities are communicated by the firm. Since firm personnel would already be notified of changes to restricted entities based on paragraph .34b, reviewing the list of restricted entities does not provide any effective response to achieving the quality objective. We recommend that .34d(2) be deleted.

- Paragraph .34e(3) of QC 1000 adds certification requirements for firm personnel, beyond the existing requirements for members of SEC Practice Section (SECPS), upon changes in personal circumstances. While quality responses are necessary when a quality risk exists related to changes in personal circumstances, other quality responses may be equally or more effective than certification in these circumstances. For example, a personal independence compliance audit may be performed when an employee is promoted to partner which would identify and resolve any financial interests in a restricted entity resulting from the change in role. We recommend QC 1000 allow firms to develop quality responses based on their unique quality risks when personal status changes rather than requiring certification upon changes in personal circumstances as a quality response.

28. Is the proposed specified quality response to have an automated process for identifying direct or material indirect financial interests appropriate? If not, why not? Is the proposed threshold (firms that issued audit reports with respect to more than 100 issuers during the prior calendar year) appropriate? If not, why not?

As discussed previously, we do not believe specified quality responses are necessary to achieve the objectives of QC 1000. However, we acknowledge that SECPS membership requirements (and existing PCAOB QC standards) provide that firms with more than 500 issuer audit clients operate an automated system to identify investment holdings of partners and managers in the firm that might impair independence, and we do not object to the proposed requirement that a firm's quality response for firms with more than 100 issuer audit clients include an automated process for identifying direct or material indirect financial interests.

If the final standard includes a specified quality response for an automated system, we request clarification that the requirement for automated systems is solely related to those processes for identifying direct and material indirect financial interests. The note to paragraph .34a of QC 1000 defines "firm and personal relationships and arrangements with restricted entities" to include employment relationships, business relationships, non-audit services, contingent fee arrangements, partner rotation, certain tax services, and arrangements requiring audit committee pre-approval, which appears to possibly require automation of processes over a broader population of relationships than direct and material indirect financial relationships. We believe processes to identify certain of the relationships described in the note to paragraph .34a, such as employment, business, and contingent fee arrangements, do not necessitate automation to achieve the related quality objective, and in some cases, there may not even be an automated solution that fully achieves the quality objective.

29. Is the proposed specified quality response related to communication of changes to the list of restricted entities at least monthly (and more frequently, if appropriate) to firm personnel and others performing work on behalf of the firm who are subject to independence requirements appropriate? Could communication to a more limited group accomplish the goal of alerting all individuals whose actions and relationships are relevant to independence? If so, to whom should changes be communicated?

As discussed previously, we do not believe specified quality responses are necessary to achieve the objectives of QC 1000. We believe timely communication of changes to the list of restricted entities is important to achieving the independence quality objectives. However, if the Board believes a specified quality response over communication of changes to the list of restricted entities is necessary, such requirements should be limited to firm personnel subject to independence requirements and allow for flexibility in the nature, timing and extent of communications. We recommend QC 1000 allow firms to develop quality responses to determine the scope, and cadence of the communication, based on the assessment of quality risks.

Engagement Performance

34. Should we include specified quality responses for the engagement performance component? If so, what should they be?

We agree with the Board's approach to not prescribe specified quality responses for the engagement performance component. We believe a firm's risk assessment process will identify the population of potential quality risks related to engagement performance for which the firm will design and implement appropriate responses.

35. We are proposing to eliminate the current Appendix K requirement and rely exclusively on a risk-based approach. Should the standard include specified quality responses explicitly directed to non-U.S. firms that audit issuers? If so, what are they?

We support a QC standard that relies on a risk-based approach as proposed. We do not believe the standard should include specified quality responses explicitly directed to non-U.S. firms that audit issuers.

Resources

39. Should the proposed standard include a specified quality response that would require the use of technological resources by the firm to respond to the risks related to the use of certain technology by the firm's clients? If yes, what should the requirement be?

We agree with the Board's approach to not include a specified quality response that would require the use of technological resources by the firm to respond to the risks related to the use of certain technology by the firm's clients. The quality objectives in QC 1000 are sufficient to allow for the continual improvement of where technology is used in the firm's QC system and provides an appropriate framework for the firm to design responses to the risks that may be introduced by technology. A principle-based, scalable standard best aligns with the rapid pace of technological advances.

Information and Communication

41. Is the proposed quality objective addressing the firm's external communications about firm-level and engagement-level information appropriate? If not, what changes to the quality objective are necessary?

We support a quality control standard that includes explicit quality objectives regarding information communicated by firms to external parties. However, we believe that the proposed quality objective in paragraph .53e regarding the firm's external communications about firm-level and engagement-level information should be limited to information resulting from and regarding the firm's evaluation of its QC system. As proposed, firms would have to establish a specific quality objective that covers all information shared regardless of form and type. This includes, but is not limited to, firm-level and engagement-level information shared through publications, including marketing material focused on promoting various service offerings, panel discussions, and presentations. We are concerned regarding firms' ability to practically design and implement quality responses to address the risk of every type and form of information communicated given the broad scope and varying modalities for such communications. We believe that limiting the requirement to information resulting from and regarding the evaluation of the firm's QC system will allow firms to focus efforts on the information that is most meaningful to relevant stakeholders, which in turn will enhance the reliability of such information.

42. Are the proposed quality objective and specified quality response addressing information and communication related to other participants appropriate? If not, why not, and what changes are necessary?

We propose that the quality objective in paragraph .53g, which addresses information and communication related to other participants that are firms, be modified to limit the extent of information shared to only what is necessary for firms to achieve the reasonable assurance objective of QC 1000. As proposed, firms will be required to obtain and consider the conclusion of the most recent evaluation of the QC system of the other participant firm and a brief overview of remedial actions taken and to be taken. We agree with firms obtaining and considering the other firm's overall conclusion of the most recent evaluation of the QC system; however, we do not believe this information should include information regarding deficiencies, if any, and remedial actions taken and to be taken. Obtaining this additional information poses legal and regulatory concerns, which we further discuss in our response to question 43 below. We believe that a requirement to obtain the overall conclusion for the most recent QC evaluation coupled with the

existing auditing standards related to the supervision and review of other participants in the performance of an engagement are sufficient and appropriate.

43. Are there legal or regulatory concerns regarding other participant firms sharing the most recent evaluation of their QC system and a brief overview of remedial actions taken and to be taken? If so, please specify.

We believe that other participant firms sharing information on their most recent evaluation of their QC system and including in that communication a brief overview of remedial actions taken and to be taken would result in the risk of communicating information included in the non-public Part II of PCAOB inspection reports. Sharing such information is inconsistent with the intent of Congress reflected in the provisions of Section 104(g)(2) and 105(b)(5)(A) of the Act. These provisions evidence a determination that confidential information about a firm's QC system and inspection and investigative matters are not matters for disclosure to audit committees, investors and the public, until such time as a firm fails to address or remediate a QC system deficiency for 12 months. We believe that our recommendation to limit the information shared to the overall conclusion of the most recent evaluation of the QC system addresses these concerns.

Monitoring and Remediation Process

45. Are the proposed requirements for the monitoring and remediation process appropriate? Are changes to the requirements necessary for this process? If so, what changes should be made and why?

We seek clarification on the expectations of an appropriate quality response for the requirement in paragraph .68d that requires a firm, when an *engagement deficiency* is determined to exist, to "evaluate whether similar *engagement deficiencies* exist on: (1) Other in-process engagements, or would arise if remedial action is not taken; (2) Other completed *engagement*s, unless it is probable that the *engagement* report(s) are not being relied upon; and (3) Work performed by the firm on other firms' engagements."

Specifically, the expectation of what "evaluate," as used in QC 1000, may require is not clear. For example, when an engagement deficiency is identified, is the expectation that an immediate evaluation be performed for *all* PCAOB engagements in the firm's portfolio that are either in-process, completed and probable that the report is being relied upon, or performed by the firm on other firms' engagements? We believe it would be appropriate for the evaluation to be limited to certain engagements based on a risk-based assessment taking into consideration the root cause of the identified engagement deficiency, such as focusing on engagements executed by certain partners, or engagements in certain industries.

To further illustrate, the example provided in the Release in section K.1.h.iv. states "if engagement team members did not comply with PCAOB standards when auditing accounts receivable because they failed to perform certain procedures in the firm's audit program, the firm could evaluate whether the person(s) who were responsible for performing the procedures and the person(s) supervising the work participated in any other audit engagement's accounts receivable testing, and if so, whether similar engagement deficiencies exist." This suggests that the extent of evaluation necessary to meet the requirement in QC 1000 would be limited to other engagements of the same people responsible for the engagement deficiency. However, since the commentary in the Release is not part of the standard and the description in the Release is only an example, the Board's intentions about the extent of evaluation necessary to achieve the Board's expectation is not clear. For the firm to "evaluate" whether similar engagement

deficiencies exist on those engagements, it may be interpreted that *all* PCAOB engagements within the firm's portfolio must then be assessed, perhaps through inspections or other means, without regard to consideration of the results of a root cause analysis to determine the likelihood of an identified engagement deficiency indicating the presence of another engagement deficiency. If the root cause of the identified engagement deficiency is not expected to be considered when satisfying the proposed requirements under paragraph .68d, we are concerned that the extensive time and effort needed to evaluate the firm's entire portfolio of in-process and completed PCAOB engagements whenever an engagement deficiency is identified on any engagement may unnecessarily detract a firm's focus from ongoing audit quality, would not be able to be operationalized without undue cost, may prevent the completion of audits of entities unrelated to the audit where the engagement deficiency originated, and is not commensurate with the potential benefits to quality. Further, the ability for a firm to scale its response to the assessed risk of a potentially pervasive root cause of a deficiency is diminished if this specified response to an engagement deficiency, as proposed, is included in the adopted standard. Should the requirements under paragraph .68d be retained in the final QC standard, we would appreciate additional clarification and guidance from the PCAOB on the expected quality response. Alternatively, we recommend that the risk-based root cause analyses, as described in paragraph .73, serve as a sufficient requirement to assess the potential for similar engagement deficiencies on other firm engagements.

46. Is the proposed requirement to inspect engagements for each engagement partner on a cyclical basis appropriate? If not, why not?

We agree inspecting engagement partners on a cyclical basis is appropriate and believe that an inspection selection process that incorporates more unpredictability and risk-based monitoring activities increases the effectiveness of the monitoring. Accordingly, we are not supportive of the expected three-year minimum cycle noted in QC 1000 because a stated expected minimum cycle may have the unintended consequence of reducing the level of unpredictability and decreasing the frequency of other such monitoring activities, such as in-process reviews. Many in the profession are implementing effective pre-issuance monitoring programs that can be more effective than post-issuance inspection. Including a three-year threshold, even with the rebuttable presumption, will quickly outdate the standard and/or inadvertently curb investment and innovation in pre-issuance monitoring programs. Recognizing the PCAOB staff already has, and will retain under QC 1000, the ability to criticize a firm's inspection and monitoring programs, we believe it would be best if the Board allows for the ability to consider the totality of the programs rather than be tethered to a presumptive period. We believe that the principle-based monitoring requirement from ISQM 1 appropriately imposes the requirement to inspect on a cyclical basis, while not deterring the incorporation of other monitoring activities. Specifically, ISQM 1 paragraph A152 states that "The nature and extent of these monitoring activities, and the results, may be used by the firm in determining: […] How frequently to select an engagement partner for inspection." We believe that linking the results of other monitoring activities to the cyclical requirement in QC 1000 would encourage an array of monitoring activities that would result in a higher quality QC system.

Relatedly, we also note that "engagements" in QC 1000 is defined as "(1) Any audit, attestation, review, or other engagement under PCAOB standards performed by a firm; or (2) Any engagement in which a firm "play[s] a substantial role in the preparation or furnishing of an audit report" as defined in PCAOB Rule 1001(p)(ii)." We believe that audit quality should consistently be measured for all engagements whether performed under the PCAOB standards or other auditing standards, and therefore, a firm's QC system should provide reasonable assurance of performing all engagements in compliance with applicable laws and professional requirements,

irrespective of the standards under which those engagements are performed. We therefore encourage the Board to consider whether the term "engagements" used in the various monitoring related requirements in QC 1000, which limits the population to only include those performed under the PCAOB standards, may result in a lost opportunity to fully capitalize on the expected benefits of a more comprehensive monitoring program.

53. Are the proposed definitions for "engagement deficiency," "QC finding," and "QC deficiency" sufficiently clear and appropriate? If not, what changes should be made and why?

We agree with the proposed definition of "engagement deficiency" and "QC finding." However, we offer a modification to the proposed definition of "QC deficiency" because the concept of "reduced likelihood" could imply a much lower threshold compared to Other QC Standards for concluding a QC finding is a QC deficiency, which creates a significant difference to ISQM 1 and SQMS 1. Such a difference would require firms to perform separate evaluations that will likely lead to different conclusions under different standards for the same circumstances. We believe this may introduce unnecessary complexity for investors and other stakeholders as reconciling such differences may not be possible or easily understood. We suggest revising the definition of a QC deficiency to align with the definition in ISQM 1 which anchors to reducing the likelihood to an acceptably low level.

Relatedly, we observed there are instances where multiple terminologies are used within the proposal to describe the same or a similar concept. For example, the definition of "major QC deficiency" introduces the concept of "significant engagement deficiencies" from PCAOB AS 1220 *Engagement Quality Review* and it is not clear how the definition of "significant engagement deficiencies" is intended to align with, or differ from, the other types of engagement deficiencies described in QC 1000. Based on our interpretation, it appears that all "engagement deficiencies where the auditor did not obtain sufficient appropriate audit evidence to support the auditor's opinion" (i.e., Part I.A findings) would be considered significant engagement deficiencies under section (1) of its definition which states "the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB or failed to perform interim review or attestation procedures necessary in the circumstances." However, we further note in the Release the Board explains "engagement deficiencies" include "instances of noncompliance in which a firm did not adequately support its opinion – because the firm did not perform sufficient procedures, obtain sufficient appropriate evidence, or reach appropriate conclusions with respect to relevant financial statement assertions." We believe this overlap in definitions between "engagement deficiencies" and "significant engagement deficiencies" creates unnecessary complexity and confusion; in particular, clarification in this regard is necessary to avoid potential inconsistent application of QC 1000. Namely, depending on whether the Board's intention is for Part I.A findings to equate to "engagement deficiencies" or "significant engagement deficiencies" that may result in different evaluation process within the proposed QC 1000 framework. For example, if Part I.A findings considered "engagement deficiencies," the firm would conduct a severity assessment and determine whether the QC finding is a QC deficiency; however, if Part I.A findings are considered "significant engagement deficiencies," then their assessment would circumvent the engagement deficiency evaluation as they are presumed circumstances of "major QC deficiencies" under paragraph .A6 of QC 1000.

Accordingly, we recommend the Board reconsider consistency of terminologies used within QC 1000 when explaining the same or a similar matter (e.g., an instance of the engagement team not obtaining sufficient appropriate audit evidence to support the auditor's opinion), and potential

alignment with terminologies used by the PCAOB in other mediums, such as inspection reports, and to the extent possible, alignment with the Other QC Standards.

Evaluating and Reporting on the QC System

57. Is November 30 an appropriate evaluation date for firms to conclude on the effectiveness of the QC system? Is there another specific date that would be more appropriate and if so, what date? Should firms be permitted to choose their own evaluation date?

In the Release, the Board acknowledges that it received several suggestions from the Concept Release indicating a future standard should provide flexibility by letting firms decide their annual evaluation date. We continue to support the position of allowing firms to choose their own evaluation date as it allows firms to align their evaluation date with ISQM 1 and key operational activities and reporting dates. For example, certain firms may need to evaluate their QC system more frequently than annually due to significant operational changes such as a firm merger. We believe that flexibility in choosing the evaluation date is best aligned with promoting a high-quality QC system and providing timely and relevant information about a firm's QC system to stakeholders as further discussed below.

Firms that have implemented other QC standards, including ISQM 1, have likely chosen an evaluation date other than November 30, that is appropriate for their business cycle, such as the fiscal year end as it aligns with operational activities, including personnel performance and compensation activities that are often aligned with a firm's fiscal year. Since ISQM 1 does not permit an evaluation period longer than 12 months, QC 1000's proposed evaluation date would require firms to perform two assessments in the year QC 1000 is adopted which is unnecessarily burdensome on firms and would result in costs that exceed the expected benefits.

Additionally, a specified date will conflict with annual reporting in other jurisdictions. For example, the European Union Transparency Directive and Regulation requires a firm's transparency report to be published at the latest four months after the firm's fiscal year end. This likely creates a gap period to a firm's November 30 QC system evaluation date and could cause a firm's transparency report to be stale or potentially published before the completion of a firm's annual evaluation of its QC system.

Paragraph .53g(2) indicates, "With respect to *other participants* that are firms, information to be obtained should include the conclusion of the most recent evaluation of the QC system of the *other participant* firm and a brief overview of remedial actions taken and to be taken." Most of a firms' audit engagements likely have calendar year-ends for which an evaluation date of November 30 and a reporting date of January 15 as proposed by QC 1000 would not provide them sufficient time to assess and respond to the participating firms' conclusions on the effectiveness of their QC system. For example, a November 30 date would likely not allow a firm time to determine the impact a participating firm's adverse conclusion may have on the nature and extent of supervision and review of the participating firm's work.

In the Release, the PCAOB indicates the proposed evaluation date is based on its understanding that many firms perform their internal inspections process during the second and third quarters of a calendar year, which allows them time to design and implement remediation efforts ahead of the next cycle of audit reports being issued on calendar year end financial statements. Firms often time their internal inspections to align with the times in their business cycle for which adequate resources can be devoted to the inspection activities. These monitoring and

remediation efforts are critical to audit quality and requiring a November 30 evaluation date does not allow sufficient time for the completion of such remediation efforts and creates an unnecessary competing priority during a period of existing heavy workloads. Further, inspection activity is only one component of the entire QC system and the entirety of the activities required to operate a high-quality QC system should be taken into account when selecting the evaluation date. We believe allowing firms the flexibility to determine their own annual evaluation date best aligns with promoting quality in audits and a firm's QC system, considering operational cycles as well as engagement performance and inspection cycles.

58. Is the proposed definition of "major QC deficiency" clear and appropriate? If not, what changes should be made and why?

No, we do not believe the proposed definition of "major QC deficiency" to be appropriate. We are primarily concerned with two aspects of the term:

- The focus on unremediated QC deficiencies. We recognize this is an intentional difference from the current framework that takes into consideration whether substantial good faith progress has been made towards remediation when evaluating the overall QC system. While firms continuously strive to remediate QC deficiencies in a timely manner, given the broad reaching nature of QC elements, the remediation of QC deficiencies often takes some period of time. This is due to the need to perform a root cause analysis, design a response, implement the responses on annual audits or into the firm's QC system and then test and evidence operating effectiveness before concluding that a QC deficiency is remediated.

  Further, our understanding of the proposal is that the PCAOB would expect that unremediated Part II comments would be presumed to be a major QC deficiency. In most cases, the PCAOB will not provide the Part II comments at the very beginning of a QC cycle. It is likely that there will be scenarios where the PCAOB issues Part II comments with only a short time before the firm is required to perform its QC evaluation (or subsequent to the annual evaluation date but prior to the Form QC reporting date) and there will not be time for the firm to fully remediate, including testing, the Part II comment by the time it must form its evaluation conclusion and report on Form QC.

  Therefore, we believe the current framework with a 12-month remediation assessment period prior to disclosure to audit committees and others becoming required, as afforded by Section 104(g)(2) of the Act which focuses on substantial good faith progress instead of complete remediation is necessary and should be retained, and will help prevent potential confusion to capital market participants that will result when different information about a firm's QC system is reported by the firm and the PCAOB in its inspection reports of the firm.

- Reference to a threshold other than "achieving reasonable assurance." We believe a QC system evaluation conclusion under Other QC Standards that "a QC system does not provide reasonable assurance that the objectives of the QC system are being achieved" is appropriate and sufficient. Therefore, it is unclear why a new term, "major QC deficiency," would be necessary, particularly when the term is focused on a threshold of "severely reduces the likelihood of the firm achieving the reasonable assurance objective." If, in application, the PCAOB intends for the definition of major QC deficiency to be the same as the Other QC Standards, we believe that is unclear in both the definition provided and in the presumptions of what belongs in that category.

> This is particularly true if, as highlighted above, the focus is on unremediated QC deficiencies because, in essence, there will be four categories that an audit firm will need to be concerned with: QC findings; QC deficiencies; Part II findings, including those that the firm is attempting to make substantial good faith progress on remediation and those that have been or will be released publicly; and major QC deficiencies. The fact that the last two categories are not in sync, and that the categories do not align with the Other QC Standards, is problematic. Please refer to our response to question 70 for further perspective.

Considering the aforementioned, we respectfully suggest the Board reconsider an evaluation and reporting framework that allows for consideration of substantial good faith progress made towards remediation, consistent with the existing framework under the Act, as well as alignment with Other QC Standards that focuses on whether reasonable assurance was achieved. Specifically, we suggest, if the terminology is retained, the Board revises the definition of a "major QC deficiency" to incorporate when the firm has not made adequate progress towards remediation as the definition of an unremediated QC deficiency. In addition, we encourage the Board to consider including further guidance in the final standard regarding the firm's evaluation of information that rises to the attention of the firm between the evaluation date and reporting date.

59. Is it appropriate to include in the proposed definition circumstances when a major QC deficiency is presumed to exist? Are the circumstances described in the proposed definition appropriate? Should there be other circumstances that give rise to such a presumption? If so, what are they?

We do not believe including presumed circumstances in the proposed definition of a major QC deficiency are appropriate. We encourage the Board to allow for a principle-based approach instead of including such prescriptive requirements. The factors presented in paragraph.78 will effectively achieve the objective of evaluating the severity of unremediated QC deficiencies. In particular, factors .78a(4) and .78a(5) are very similar to certain aspects of the presumed situation of unremediated QC deficiencies that "results in or is likely to result in one or more significant engagement deficiencies in engagements that, taken together, are significant in relation to the firm's total portfolio of engagements conducted under PCAOB standards." Accordingly, we recommend the Board to remove the presumed circumstances altogether in addition to aligning the definition of major QC deficiency consistent with our response to question 58.

61. Should firms be required to report on the evaluation of the QC system to the PCAOB? If not, why not?

We support firms reporting to the PCAOB on the annual evaluation of their QC system and agree it is appropriate for the reporting on Form QC to be non-public.

63. Is the proposed date for reporting on the evaluation of the QC system (January 15) appropriate? Is there another specific date that would be more appropriate and if so, what date? Is 45 days after the evaluation date an appropriate reporting date?

As noted in the response to question 57, we believe firms should be able to choose their own evaluation date and therefore believe the reporting date should not be a specific date, but rather a defined period after the firm's evaluation date. We also believe that the proposed reporting date of 45 days after the evaluation date does not provide sufficient time to complete the assessment, given the size, volume and scope of firms' QC systems. We recommend considering aligning with other established reporting timelines, for instance, the PCAOB Form 2 provides for a 90 day reporting period.

We note that paragraph .84 of QC 1000 sets the documentation completion date as the same date as the reporting date which differs from the reporting and documentation structure of the auditing standards. Namely, AS 1210.15 requires documentation completion to occur no more than 45 days from the report release date. While we do not believe a full 45 days is necessary to assemble a complete and final set of documentation, there is some time required between reaching the evaluation conclusion, reporting and assembling the final set of documentation. If the final standard retains the same date for documentation completion and reporting, we suggest that when evaluating the length of the reporting period, the time needed to assemble documentation is factored into the determination of the reporting period in the final standard.

64. Rather than reporting on Form QC, should firms report on the evaluation of the QC system, as of March 31 on a non-public portion of Form 2, which is due on June 30?

As noted in our response to question 57, we believe allowing firms to choose their own evaluation date is the most preferable as it allows firms to align their evaluation date with key operational activities and reporting dates, and we believe is best aligned with promoting a high quality QC system. Although an evaluation date of March 31 would bring many of the same challenges and retain many of the same concerns as an evaluation date of November 30, if the Board believes the benefits of consistent dates among firms outweighs the drawbacks as discussed elsewhere in this response letter to have a consistent evaluation date, we believe an evaluation date of March 31 is preferable to November 30.

66. Are proposed Rule 2203A, *Report on the Evaluation of the Firm's System of Quality Control*, and the proposed Form QC instructions included in Appendix 2, clear and appropriate? If not, why not?

The proposed Form QC instructions includes three evaluation conclusions that firms can reach:

- Effective with no unremediated QC deficiencies;
- Effective, except for one or more unremediated QC deficiencies that are not major QC deficiencies; or
- Not effective (one or more major QC deficiencies exists).

As proposed, firms can reach and report different evaluation conclusions under QC 1000 compared to the Other QC Standards for the same set of circumstances. As noted in the Release, the Board acknowledges that "there may be circumstances in which a firm would conclude under QC 1000 that its QC system was ineffective, but still view its QC system as providing reasonable assurance for purposes of Other QC Standards." Such instances of differing conclusions between QC 1000 and ISQM 1 or other standards may inadvertently adversely impact U.S. investors' decisions, as they may misinterpret the risk profile between the jurisdictions; which, in turn, adversely impact the U.S. capital markets. Certain firms that would be subject to the requirements of QC 1000 will reasonably be expected to have instances of concluding that the firm's QC system is effective, except for (i.e., the second conclusion above), while firms reporting under the Other QC Standards will have a conclusion that the QC system is effective. This may improperly imply concerns regarding audit quality for firms that are subject to the requirements of QC 1000. Said another way, the differing conclusions under the various standards may lead investors and other capital markets stakeholders to have the false belief there are different circumstances that lead to an "except for" conclusion, while the underlying circumstances are the same. We recommend the Board reconsider the evaluation conclusions

and align the reporting conclusions in the final QC standard with the Other OC Standards to avoid these unintended consequences of stakeholder confusion.

Additionally, proposed Rule 2203A indicates Form QC or its content may become public as part of an enforcement proceeding. Form QC or its content may not be relevant to all enforcement proceedings; therefore, we suggest the Board explicitly clarify in the final standard that the Form QC may become public as part of an enforcement proceeding where Form QC or its content is relevant to the respective enforcement proceeding.

Lastly, we recommend the Form QC instructions included in Appendix 2 include materiality thresholds and further guidance regarding what circumstances trigger an amendment to a filed Form QC. This will contribute to consistent practice across firms and align with the Board's expected use of such information.

70. Are the proposed amendments to AS 1301 that require the auditor to communicate to the audit committee about the firm's most recent annual evaluation of its QC system appropriate? If not, why not?

We are supportive of transparency in communication relating to a firm's QC system with the audit committee, to the extent the information is considered material. However, we do not believe the proposed amendment to AS 1301 achieves that objective and will compel a firm to disclose non-public QC information to audit committees which is inconsistent with the current framework established by Section 104(g)(2) of the Act. Refer to our response to question 43 above. Also, as discussed earlier in response to question 58, incorporating a sufficient period for remediation and taking such remedial actions into consideration when reaching an overall conclusion on a firm's QC system is critical. The 12-month remedial period provided under the Act has appropriately taken into consideration a reasonable period of time necessary to remediate deficiencies that are broad reaching in nature, as those within a firm's QC system. At the same time, the Act acknowledges that a failure by a firm to make progress in remediating deficiencies for 12 months is information of sufficient importance that it should be made available to audit committees and investors.

Further, the proposed amendments are inconsistent with the Board's interpretation of the Act as described in the PCAOB Release No. 2012-003 *Information for Audit Committees About the PCAOB Inspection Process*:

> By law, the Board cannot disclose to an audit committee the nonpublic portion of an inspection report or other nonpublic inspection information … and the Board cannot compel an audit firm to disclose such information to an audit committee.

One potential solution, as we discussed in our response to question 58, is to align the definition of a major QC deficiency to the threshold that the PCAOB uses to determine whether to release Part II, and then have discussions with the audit committee only around remedial actions taken and to be taken with respect to major QC deficiencies. If that was done, the Part II comments are then made public and the confidentiality provisions written into the Act would no longer apply. This has added benefits of providing consistency in information to the capital markets about a firm's QC system between the firm's reporting and the PCAOB's inspection reports and enabling firms to be more transparent in their QC system reporting.

Additionally, the proposed communication to audit committees would include more information about QC deficiencies of the firm than what an auditor is required to communicate about an

issuer's deficiencies under PCAOB AS 1305: *Communications About Control Deficiencies in an Audit of Financial Statements* and PCAOB AS 2201: *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, and what an issuer is required to communicate about its deficiencies in management's report on internal control over financial reporting under Item 308 of SEC Regulations S-K and S-B. This requirement in the proposed amendments to AS 1301 could result in misinterpretations by audit committees about the nature and severity of a firm's QC deficiencies. We believe the communications to audit committees should be limited to the conclusion of a firm's most recent annual evaluation, and upon the determination that substantial good faith progress has not been made on the remedial actions, similar to the release of such information under the confidentiality provisions under the Act, including a brief overview of remedial actions taken or to be taken. We believe communicating this information provides audit committees with sufficient decision-useful information while recognizing that audit committees are free to request further information from their auditor should they determine that additional information is necessary to fulfill their governance responsibilities.

Documentation

71. Are the proposed documentation requirements appropriate? If not, what changes should be made?

We suggest the documentation retention requirements be bifurcated between those related to (1) the annual evaluation of the firm's QC system, and (2) the operation of the firm's QC system. We agree that firms should retain documentation of the evaluation of their QC system for seven years from the QC documentation completion date. However, we believe that the requirement for firms to retain documentation evidencing the operation of the QC system for seven years will result in costs that are not commensurate with the benefits. If the requirement is retained, we respectfully recommend the PCAOB to consider such incremental costs in the Board's economic analysis. The information evidencing the operation of the firm's QC system can vary in size, type, and storage requirements. The cost of retaining such a variety of information, in the firm's existing IT infrastructure or modifying the firm's existing IT systems to comply with such a requirement would be significant. Further, retaining such a volume of information for seven years would expose firms to information security risks, which the Board should also consider. We recommend the requirement for the retention of documentation of the operation of the firm's QC system be revised to align with the documentation retention requirements for issuers under the Act.

Proposed Amendment to AS 2901, *Omitted Procedures after Report Date*

74. Is the proposal to expand the scope of AS 2901 to include engagement deficiencies on ICFR audits appropriate? If not, why not?

We support the proposed quality objective to expand the scope of PCAOB AS 2901 *Responding to Engagement Deficiencies After Issuance of the Auditor's Report* to include engagement deficiencies on ICFR audits.

75. Is it appropriate for remedial action to be required for all identified engagement deficiencies, not just in situations where the auditor's opinion may be unsupported? If not, why not?

We support the proposed quality objective which allows for scalable remedial action for all engagement deficiencies. We request further guidance regarding paragraphs .03 and .04 of the proposed amendment to AS 2901. For example, we believe further guidance, similar to what

exists in the current AS 2901 regarding the assessment of the importance of the omitted procedures, or an explicit alignment to the PCAOB definition of a Part 1.A or Part 1.B deficiency, would assist in distinguishing between the engagement deficiencies that require a response under proposed paragraphs .03 versus .04.