



June 5, 2023

Ms. Phoebe W. Brown
Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: Proposed Auditing Standard – *General Responsibilities of the Auditor in Conducting an Audit* (PCAOB Release No. 2023-001, March 28, 2023; PCAOB Rulemaking Docket Matter No. 049)

Dear Ms. Brown:

The U.S. Chamber of Commerce (“Chamber”) Center for Capital Markets Competitiveness appreciates the opportunity to comment on the Public Company Accounting Oversight Board (“PCAOB” or “Board”) Exposure Draft on *General Responsibilities of the Auditor in Conducting an Audit* (“Exposure Draft” or “Proposal”). The Proposal is part of the Board’s standard-setting agenda to update and modernize PCAOB Auditing Standards (“AS”). The Chamber supports the PCAOB’s goal to update its auditing standards with thoughtful consideration and due process.¹

This standard-setting project focuses on the general principles and responsibilities of the auditor in conducting an audit. These principles and responsibilities are foundational and encompass extant PCAOB standards on reasonable assurance, due professional care, professional skepticism, independence, competence, and professional judgment.²

According to the Executive Summary of the Proposal, the PCAOB is “reaffirming the general principles and responsibilities to ensure that the foundation continues to be solid and appropriate for maintaining high quality audits.”³ The proposed standard (“AS 1000”) and amendments would modernize PCAOB standards to “[r]eflect changes in the auditing environment; [e]liminate outdated and inconsistent language; and [a]chieve consistency with Board-issued standards.”⁴ These summarizations suggest that the Proposal is essentially a housekeeping exercise.

¹ For example, see the letters to the PCAOB from the U.S. Chamber of Commerce Center for Capital Markets Competitiveness on the PCAOB Concept Release on *Potential Approach to Revisions to PCAOB Quality Control Standards* dated March 16, 2020; the PCAOB Request for Comment on *Advisory Groups – Draft Governance Frameworks* dated February 28, 2022; and the PCAOB Request for Comment on the *Draft 2022-2026 Strategic Plan* dated August 16, 2022.

² See the Exposure Draft, page 4.

³ See the Exposure Draft, page 4.

⁴ See the Exposure Draft, page 5.

Ms. Phoebe W. Brown

June 5, 2023

Page 2

However, considering the Exposure Draft in its entirety reveals that the proposed revisions belie these benign characterizations. The Chamber is challenged to interpret the Proposal as consistent with a reaffirmation or clarification of existing standards. Rather than reaffirm and clarify, the Proposal creates confusion about the role and responsibilities of auditors; mischaracterizes the application of generally accepted accounting principles (“U.S. GAAP”) as promulgated by the Financial Accounting Standards Board (“FASB”) – which provides the financial reporting framework in Securities and Exchange Commission (“SEC”) filings and bounds the auditor’s responsibilities; promotes an expectations gap with investors; has significant attendant consequences, which lack any meaningful economic analysis; and raises a number of other concerns.

In its current form, the Chamber cannot support the Proposal as fit for purpose. The Chamber strongly urges the PCAOB to withdraw it and substantially reconsider, recraft, and re-expose a revised proposed standard on the general responsibilities of the auditor in conducting an audit.

Following a background on the U.S. financial reporting structure and framework that provides context for our concerns and recommendations, we discuss them in more detail below.

Background

It is widely recognized that reliable financial reporting is essential to well-functioning capital markets and our economy. In the U.S., market participants – regulators, standard-setters, management, boards and audit committees, internal auditors, independent auditors, securities lawyers, and the providers of capital, among others – all play a role and work together in support of reliable financial reporting.

However, it is also the case, that under the U.S. financial reporting structure, management is responsible for preparing and filing GAAP-compliant financial statements with footnote disclosures (for convenience, referred to as “the financial statements”) as required by the SEC. Management is likewise responsible for establishing and maintaining effective internal control over financial reporting (“ICFR”).

Management’s responsibility for adopting sound accounting policies, maintaining effective ICFR, and making fair representations in the financial statements contrasts with the auditor’s responsibility for verifying management’s representations.⁵ An independent audit

⁵ For example, see *Auditing & Assurance Services: An Integrated Approach (15th Edition)* by A. A. Arens, R. J. Elder, and M. S. Beasley, page 143.

Ms. Phoebe W. Brown

June 5, 2023

Page 3

increases the reliability of financial statements and ICFR information reported by management, thereby, enhancing the confidence of investors and creditors in this information.⁶

U.S. GAAP

GAAP as promulgated by FASB is the financial reporting framework for U.S. companies.⁷ In the aftermath of the Sarbanes-Oxley Act of 2002 (“SOX”), the SEC formally reaffirmed FASB as the private-sector standard setter for U.S. GAAP under SOX Section 108. Thus, FASB’s financial accounting and reporting standards are recognized as “generally accepted” for the purposes of the federal securities laws.⁸

Registrants are required to comply with FASB standards in preparing financial statements filed with the Commission. SEC Regulation S-X Rule 4-01(a)(1) states:

Financial statements filed with the Commission which are not prepared in accordance with generally accepted accounting principles will be presumed to be misleading or inaccurate, despite footnote or other disclosures, unless the Commission has otherwise provided.

The FASB Accounting Standards Codification (“Codification”) is the source of authoritative GAAP recognized by FASB for application by companies and auditors. Importantly, Topic 105-10-05-1 of the Codification explicitly provides that rules and interpretive releases of the SEC under authority of the federal securities laws are also sources of authoritative GAAP for SEC registrants. Topic 105-10-05-4 of the Codification explains that content in the SEC sections is designated by an “S” preceding the section number and provided for convenience, relates only to SEC registrants, and does not contain the entire population of current SEC rules, regulation, interpretive releases, and staff guidance.

Effective ICFR

SEC rules require management to base its evaluation of the effectiveness of ICFR on a suitable recognized control framework (also known as control criteria) established by a body or group that follows due process procedures, including the broad distribution of the framework

⁶ For example, see the Center for Audit Quality White Paper on “The Value of the Audit: A Brief History and the Path Forward” (“CAQ White Paper”) (June 2021); the “U.S. Financial Reporting Structure for Public Companies: A Blue Print” available on the SEC website under the Office of the Chief Accountant; and various statements by SEC Commissioners and staff such as the recent Statement on “Assessing Materiality: Focusing on the Reasonable Investor When Evaluating Errors” by Paul Munter, SEC Chief Accountant (March 9, 2022).

⁷ U.S. GAAP as promulgated by FASB is also used as the financial reporting framework by many Foreign Private Issuers (“FPIs”).

⁸ See the SEC Policy Statement *Reaffirming the Status of the FASB as a Designated Private-Sector Standard Setter* (Release Nos. 33-8221; 34-47743; IC-26028; FR-70) (April 25, 2003).

Ms. Phoebe W. Brown

June 5, 2023

Page 4

for public comment.⁹ The control framework promulgated by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) is the most widely used framework for ICFR-related reporting in SEC filings.

Reasonableness

Reasonableness is a core principle of the U.S. financial reporting framework. For example, management is responsible for maintaining books and records in reasonable detail and maintaining a system of ICFR that provides reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.¹⁰ “Reasonable detail” and “reasonable assurance” are defined as the level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own affairs.¹¹

Financial statement audits and integrated audits of the financial statements and ICFR provide reasonable assurance. The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the GAAP financial statements are free of material misstatement, whether caused by error or fraud, (i.e., “fairly presented”) and, in an integrated audit, whether effective ICFR was maintained in all material respects. Reasonable assurance is a high level of assurance – it is not absolute assurance. The auditor is not an insurer or guarantor.

Reasonableness also applies to the judgments inherent in accounting and financial reporting in accordance with U.S. GAAP, the application of COSO to ICFR, and auditing in accordance with PCAOB rules and standards. For example, accounting and financial reporting judgments by management include selecting and implementing the accounting standards to account for transactions and events; estimating the amount to record; evaluating the sufficiency of evidence; and deciding on financial statement presentation and footnote disclosures.¹² Likewise, professional judgment is inherent in all phases of the audit – from deciding on client acceptance and retention; through planning and conducting the engagement, obtaining sufficient appropriate evidence, and rendering an opinion; to documenting the process and result.

Overarching Concern with the Proposal

⁹ See AS 2201 on *The Audit of Internal Control Over Financial Reporting that is Integrated with An Audit of Financial Statements*, footnote 7.

¹⁰ For example, see the Foreign Corrupt Practices Act (Sections 13(b)(2)(A) and (B) of the Exchange Act) and SEC *Guidance Regarding Management’s Report on Internal Control Over Financial Reporting Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934* (“Management Guidance”) (June 27, 2007).

¹¹ For example, see the Exchange Act Section 13(b)(7).

¹² See the *Final Report of the Advisory Committee on Improvements to Financial Reporting to the United States Securities and Exchange Commission* (August 1, 2008), pages 89-91.

This background provides context for discussing the Chamber’s concerns about the Proposal and how it undermines the U.S. financial reporting structure and framework. In addition, the current regulatory environment for auditors, including the Board’s focus on enforcement as a primary tool of the PCAOB,¹³ helped inform our perspectives on the Proposal, as reflected in the subsequent discussion.

We also considered the Proposal in light of the goals and objectives for standard-setting in the PCAOB’s Strategic Plan (“Plan”). The Plan calls for modernizing PCAOB standards, not just to meaningfully improve audit quality, but to enhance the PCAOB’s ability to enforce standards and inspect for compliance.¹⁴ Unfortunately, the Proposal will have very little practical effect on the former and primarily focuses on the latter.

Whether by accident or design, the proposed revisions and amendments in standards on the general responsibilities of the auditor – both individually and collectively – are not likely to improve audit quality. Rather, the Proposal will significantly increase the risks for audit firms and individual auditors, including engagement partners, of PCAOB inspection findings, PCAOB enforcement, SEC enforcement, and private securities litigation, along with attendant reputation effects.

Further, the Board’s focus on enhancing inspection findings and enforcement, including against engagement partners, may have additional unintended consequences that will have long-lasting adverse impacts on the profession. Attracting and retaining high quality talent has always been an important priority for the profession. But the challenges of doing so have been greater in the last few years. The Proposal may exacerbate these challenges. The Chamber is very concerned that the Proposal will contribute to undermining the attractiveness of the audit profession, which extends to the willingness of individuals to serve as engagement partners on issuer and broker-dealer audits.

These are a few of the important consequences that require robust economic analysis and full consideration by the Board. Such analyses and considerations are absent from the Proposal. Instead, the Proposal contains very limited economic analysis that concludes: “Overall, we expect that the economic impacts of the proposed changes, including both benefits and costs, would be relatively modest ...”¹⁵ While the benefits of the Proposal are likely modest, the costs are not.

¹³ For example, see the PCAOB Media Advisory and video on Chair Williams Keynotes Baruch Conference on Financial Reporting (May 4, 2023).

¹⁴ See the *PCAOB Strategic Plan 2022-2026*, page 10.

¹⁵ See the Exposure Draft, page 45.

Ms. Phoebe W. Brown

June 5, 2023

Page 6

The costs that have not been analyzed – either quantitatively or qualitatively – include the costs to audit firms from the new legal duties and auditor responsibilities created by the Proposal, as subsequently discussed. Moreover, the ensuing costs of the Proposal will impact issuers and broker-dealers through increased audit fees, which likewise have not been analyzed or considered.

The inadequacy of the economic analysis and consideration of consequences – both intended and unintended consequences – necessitates that the PCAOB withdraw and reconsider the Proposal.

We next address the PCAOB’s claim that the auditor’s responsibilities on financial statement audits are not bound by GAAP and that “mere” compliance with GAAP is not sufficient.

GAAP Bounds the Auditor’s Responsibility to Evaluate Fair Presentation of a Company’s Financial Statements

The Chamber is very concerned that the PCAOB is using the Proposal as an attempt to remove the financial reporting framework of U.S. GAAP as the boundary for the auditor’s responsibilities in rendering opinions on financial statements. For example, the narrative (release) text of the Proposal states:

[t]he amendments would clarify that the auditor’s evaluation of fairness goes beyond the evaluation of whether the financial statements are presented in conformity with the applicable financial reporting framework. U.S. federal securities laws prohibit the financial statements and company disclosures from being materially misleading, which is a broader concept than mere compliance with the applicable financial reporting framework. Presented fairly, under extant PCAOB standards, is a parallel concept that goes beyond mere technical compliance with the applicable financial reporting framework. However, the existing standards may not be sufficiently clear that the auditor’s obligation concerning the fairness of the financial statements extends beyond compliance with the applicable financial reporting framework.¹⁶

Otherwise, the Proposal provides no additional discussion of this matter.

The Chamber is puzzled by the claim that “existing standards may not be sufficiently clear ...” Existing PCAOB standards appear to be a model of clarity. To illustrate, currently PCAOB AS 2815 on *The Meaning of “Present Fairly in Conformity with Generally Accepted Accounting Principles”* states:

¹⁶ See the Exposure Draft, page 30.

Ms. Phoebe W. Brown

June 5, 2023

Page 7

*The independent auditor's judgment concerning the 'fairness' of the overall presentation of financial statements should be applied within the framework of generally accepted accounting principles. Without that framework, the auditor would have no uniform standard for judging the presentation of financial position, results of operations, and cash flows in financial statements.*¹⁷

The Proposal calls for deleting this provision from PCAOB auditing standards.¹⁸

Adding to the puzzle, the proposed revisions in the meaning of “fairly present” were stealth-like, as only Board Member Stein referred to them during the open Board meeting.¹⁹ Otherwise, to discern the proposed revisions required reading the entire Exposure Draft. However, matters crystalized when the PCAOB issued an Investor Bulletin to market the Proposal to investors. The Bulletin said:

*The Board's proposal, if adopted, would ...clarify that the auditor's responsibility to evaluate the fair presentation of a company's financial statements is a broader concept than mere compliance with the applicable financial reporting framework (such as U.S. GAAP).*²⁰

Unfortunately, “clarify” cannot be used to describe a core responsibility that does not now exist.

Perhaps this is why Board Member Stein referred to the proposed revisions as an “enhancement.” Even so, “enhancement” likewise understates the import of such a sea-change in the auditor’s responsibilities. Irrespective of semantics, such a proposal is conceptually flawed, practically unworkable, lacks any economic analysis by the PCAOB, and contributes to an expectation gap with investors.

To elaborate, the Proposal would also amend AS 2810 on *Evaluating Audit Results* to add a footnote to paragraph AS 2810.17 on the evaluation of the effect of uncorrected misstatements. The proposed footnote reads:

¹⁷ See the deleted text in the Exposure Draft, page A2-3.

¹⁸ The Proposal deletes additional language in AS 2815 on the meaning of “present fairly” that should be retained. This includes language in paragraph AS 2815.04 such as “... within a range of acceptable limits, that is, limits that are reasonable and practicable to attain in financial statements.”

¹⁹ Board Member Stein’s statement, posted on the PCAOB website, says: “The proposal enhances an auditor’s evaluation of the presentation of the financial statements. This includes requiring an auditor’s determination of whether additional information or disclosures, beyond those required by the financial reporting framework, may be necessary.” See “A Return to Roots: General Responsibilities of the Auditor in Conducting an Audit” by Kara M. Stein, Board Member, at the PCAOB Open Board Meeting (March 28, 2023).

²⁰ See the PCAOB Investor Bulletin on an *Opportunity to Comment on Proposed Standard Addressing Core Auditing Principles and Responsibilities* (April 17, 2023).

For additional considerations regarding the fairness of presentation of financial statements, see, e.g., SEC Rule 12b-20.17, C.F.R. [par.]240.12b-20 (requiring issuers to disclose “in a statement or report ... such further information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made not misleading.”).²¹

It is instructive to recognize that Section 240 of the Code of Federal Regulation (“CFR”) involves the “General Rules and Regulations, Securities Exchange Act of 1934.” Paragraph 240.12b-20 (“Rule 12b-20”) is a longstanding provision on “Additional Information” that deals with material omissions in SEC filings. It states:

In addition to the information expressly required to be included in a statement or report, there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made not misleading.

Rule 12b-20 applies to filings with the SEC (i.e., annual Form 10-Ks and quarterly Form 10-Qs) in their entirety. In applying to SEC filings broadly, Rule 12b-20 falls under the purview of the securities lawyers that advise management. Auditors are not expected to be experts in the securities laws.²²

Moreover, PCAOB auditing standards distinguish between the auditor’s responsibilities related to the financial statements and the auditor’s responsibilities related to other information in documents containing audited financial statements such as 10-Ks and 10-Qs. The latter standard, which the PCAOB is not proposing to amend, states:

The auditor’s responsibility with respect to information in a document does not extend beyond the financial information identified in his report, and the auditor has no obligation to perform any procedures to corroborate other information contained in a document. However, he should read the other information and consider whether such information, or the manner of its presentation is materially inconsistent with information, or the manner of its presentation, appearing in the financial statements.²³

²¹ See the Exposure Draft, page A2-2.

²² It is noteworthy that the proposed changes would place auditors “in the shoes of management” (and the securities lawyers that advise management) to assess SEC 10-K and 10-Q filings in their entirety, as to whether additional information is necessary to make the filing not misleading. Such a move contravenes SEC and PCAOB auditor independence rules, too.

²³ See PCAOB AS 2710.04 on *Other Information in Documents Containing Audited Financial Statements*.

However, the PCAOB's claims are flawed setting aside these considerations and the proposed footnote. SEC rules that involve GAAP reporting do not remove U.S. GAAP as the boundary for auditor responsibilities. As previously discussed, as an additional source of authoritative GAAP for SEC registrants, the FASB Accounting Standards Codification (i.e., U.S. GAAP) encompasses SEC rules, regulations, and interpretive releases for financial statement presentation and footnote disclosure. The PCAOB should not attempt to create auditor responsibilities out of an oxymoron.

Further reinforcing compliance with GAAP as the boundary for fair presentation of the financial statements, auditors cannot override GAAP under PCAOB rules and standards. To explain, Rule 203 (now Rule 2.320.030) of the Code of Professional Ethics of the American Institute of Certified Public Accountants ("AICPA") permits an unqualified opinion on financial statements that departs from GAAP under certain, very limited circumstances. While the use of this "GAAP override" rarely occurs in audits of private companies, it does not apply at all to audits overseen by the PCAOB – as the PCAOB has never adopted Rule 203 or an equivalent.²⁴ Compliance with U.S. GAAP is both necessary and sufficient for the auditor to render an unqualified opinion on financial statement audits of issuers and broker-dealers.²⁵

To summarize, GAAP as promulgated by FASB is the financial reporting framework for U.S. companies. The auditor expresses an opinion about whether the financial statements comport with GAAP in all material respects – which is the meaning of "fairly present." The differing responsibilities of management and auditors under the U.S. financial reporting structure are, nonetheless, aligned based on GAAP as the framework for financial statement presentation and footnote disclosure. This alignment makes both conceptual and practical sense.

In this regard, the Proposal raises significant issues for companies (i.e., issuers and broker-dealers). It is essential to recognize that the PCAOB's proposed changes in the auditor's responsibilities, by extension, likewise eliminate U.S. GAAP as the boundary for management's responsibilities. Clearly the PCAOB does not have the authority to do so. The PCAOB is swimming outside its lane.

²⁴ See PCAOB Auditing Standard 6 (AS 2820) on *Evaluating Consistency of Financial Statements and Conforming Amendments* (PCAOB Release No. 2008-001) (November 15, 2008), pages 14-15, which explains that, in 2003, when the Board adopted certain AICPA rules and Auditing Standard Board standards as interim Board standards, the Board did not adopt Rule 203.

²⁵ A proposed note to AS 2810.31 raises similar concerns, as it is untethered to GAAP, saying: "The auditor should also evaluate whether the substance of transactions or events differs materially from their form." (See the Exposure Draft, page A2-3.) The PCAOB should maintain the extant language in AS 2815.06, including the term "consider" rather than "evaluate," as follows: "Generally accepted accounting principles recognize the importance of reporting transactions and events in accordance with their substance. The auditor should consider whether the substance of transactions or events differs materially from their form."

Ms. Phoebe W. Brown

June 5, 2023

Page 10

Importantly, the Proposal fails to include any economic analysis of the proposed revisions and amendments to the meaning of “fairly present.” No evidence is provided to support the need for, or the costs and benefits of, the proposed revisions and amendments to remove GAAP as the boundary for the auditor’s responsibilities to evaluate fair presentation of a company’s financial statements. Regardless of whether the Proposal is described as a reaffirmation, a clarification, an enhancement, a sea-change, or simply misguided – it requires robust economic analysis.

In addition, by claiming that U.S. GAAP is not the boundary for auditor responsibilities on financial statement audits, the PCAOB is contributing to an expectation gap with investors. The PCAOB lacks the authority to overcome any investor perceptions of shortcomings in GAAP or to expect auditors do likewise – that authority resides with FASB and the SEC.

The Chamber strongly urges the PCAOB to eliminate the proposed amendment to AS 2810 (i.e., delete the proposed footnote to paragraph AS 2810.17) and maintain the substance of AS 2815.

Additional Concerns

The Chamber has a number of additional concerns with the Proposal, including proposed revisions and amendments related to the objectives of an audit, reasonable assurance, the meaning of “the financial statements as a whole,” due professional care, professional skepticism, professional judgment, and competence in addition to other matters. These concerns are discussed in more detail below.

Objectives of an Audit

Independent audits have long been required for registrants in support of the SEC’s tri-part mission to protect investors, facilitate capital formation, and maintain fair, orderly, and efficient markets. The investor protection aspect of this mission was enhanced with SOX and the creation of the PCAOB (under SEC oversight). As provided in SOX Section 101(a), the PCAOB’s mission is to:

*[O]versee the audit of public companies that are subject to the securities laws, and related matters, in order to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports for companies the securities of which are sold to, and held by and for, public investors.*²⁶

²⁶ SOX gives the PCAOB authority for registration, inspection, standard-setting, and enforcement of auditors and audits of issuers. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank”) added auditors of certain broker-dealers to the PCAOB’s inspection authority.

The Chamber appreciates the essential role of independent audits in enhancing the confidence of investors and other market participants in a company's financial statements (and ICFR on integrated audits) that underpins the PCAOB's investor protection mission.²⁷ Auditors overseen by the PCAOB should and do recognize the purpose of an audit and that investors are the primary users of the financial statements. This is part of the culture of audit firms and is reflected in auditor independence requirements and other PCAOB rules and standards.

However, the PCAOB risks misleading investors and others by stating in an auditing standard on the general responsibilities of auditors that "[a]uditors have a fundamental obligation to protect investors" and "that obligation governs the auditor's work under the standards of the PCAOB."²⁸ Rather, PCAOB rules and standards govern (i.e., control and direct) the auditor's work. Moreover, the Proposal conflates the overall benefits from independent audits for investors in our capital markets with any potential legal duties in the context of the facts and circumstances of individual audit engagements.

Our concerns are reinforced by narrative (release) text in the Proposal such as "[a]uditors have a fundamental obligation to the public by serving as the protector of the public interest in the integrity of financial statements."²⁹ Again, such overarching statements run the risk of being interpreted as creating legal or fiduciary duties for auditors to an unknown cadre of investors or the public generally.³⁰

The Chamber urges the PCAOB to delete proposed paragraph AS 1000.01. The proposed paragraph AS 1000.02 can serve as an appropriate introduction.^{31, 32}

²⁷ See the Exposure Draft, page A1-1.

²⁸ See the Exposure Draft, page A1-1.

²⁹ See the Exposure Draft, page 16.

³⁰ The PCAOB also cites a 1984 Supreme Court decision that the auditor functions as a "public watchdog" (see the Exposure Draft, page 16). However, this case arose out of an investigation of a corporation's tax returns by the Internal Revenue Service ("IRS"). And, the Exposure Draft mischaracterizes the decision, which is narrower than suggested and did not find or create any legal obligation of the nature suggested. Under provisions of the Internal Revenue Code of 1954, the IRS sought access to the tax accrual workpapers prepared by an independent audit firm, while routinely reviewing the corporation's financial statements. The corporation instructed the audit firm not to comply with an IRS summons – under some form of work-product immunity from disclosure – and the IRS sued for enforcement of the summons. The court rejected an analogy to the work-product protection available in the context of legal advice – contrasting the attorney's role as "confidential adviser and advocate" to the role of the independent auditor as a "disinterested analyst charged with public obligations" (*United States, Petitioner v. Arthur Young & Co.*, 465 U.S. 805 (1984) at 818).

³¹ See the Exposure Draft, page A1-1.

³² For the same reasons (along with others subsequently discussed), the proposed paragraph AS 1000.15 should also be deleted or reframed, as it states: "The auditor must comply with applicable professional and legal requirements in conducting an audit. In fulfilling these requirements, the auditor should keep in mind their role in protecting investors." See the Exposure Draft, page A1-6.

In addition, while we assume that it is a drafting oversight, the proposed paragraphs on the objectives of the auditor, AS 1000.03(a) and 1000.03(b), lack any reference to the relevant criteria – that is U.S. GAAP for (a) and COSO (or other suitable control criteria) for (b). As to the latter, references to ICFR throughout the Proposal likewise lack any tethering to COSO (or other suitable control criteria) and need to be reconsidered. Indeed, we could not find any mention anywhere in the Proposal of the control criteria for ICFR. Further, the Chamber suggests the PCAOB clarify that the audit of ICFR is integrated with a financial statement audit. Currently, the Proposal reads as if the PCAOB is referring to a standalone audit of ICFR.

Reasonable Assurance

As previously discussed, reasonableness is a core principle of the U.S. financial reporting framework. Consistent with this core principle, financial statement audits and integrated audits of the financial statements and ICFR provide reasonable assurance. Although the PCAOB is proposing to retain the concept of reasonable assurance,³³ the Proposal fails to include important language from existing PCAOB standards that provide transparency on the meaning of reasonable assurance – and the PCAOB fails to explain or justify this move.

The following examples of selected portions from PCAOB auditing standards that the Proposal deletes illustrate the breadth of the provisions being eliminated:

(AS 1015.10) ... Absolute assurance is not attainable because of the nature of audit evidence and the characteristics of fraud. Although not absolute assurance, reasonable assurance is a high level of assurance. Therefore, an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States) may not detect a material weakness in internal control over financial reporting or a material misstatement to the financial statements.

(AS 1015.11) ... As a result of these factors, in the great majority of cases the auditor has to rely on evidence that is persuasive rather than convincing.

(AS 1015.12) ... Because of the characteristics of fraud, a properly planned and performed audit may not detect a material misstatement. ...

(AS 1015.13) Since the auditor's opinion on the financial statements or internal control over financial reporting is based on the concept of obtaining reasonable assurance, the auditor is not an insurer and his or her report does not constitute a guarantee. Therefore, the subsequent discovery that either a material misstatement, whether from error or fraud, exists in the financial statements or a material weakness in internal control over financial reporting exists does not, in and of itself, evidence (a) failure to

³³ See the Exposure Draft, pages 27, A1-1, and A1-6.

Ms. Phoebe W. Brown

June 5, 2023

Page 13

obtain reasonable assurance, (b) inadequate planning, performance, or judgment, (c) the absence of due professional care, or (d) a failure to comply with the standards of the Public Company Accounting Oversight Board (United States).

The Chamber is concerned that failing to retain the longstanding explanatory language in AS 1015 will confuse investors about the nature of reasonable assurance. Investors may not appreciate or respect that the Proposal represents no change in the meaning of reasonable assurance. Indeed, quite the opposite, investors will likely assume that the deletions signal a change.

From an investor perspective, mentioning in the narrative (release) text of the Proposal – that reasonable assurance is attained by performing audit procedures and evaluating the resulting audit evidence in accordance with PCAOB standards – is not especially useful.³⁴ Irrespective of how it is attained, investors generally prefer that auditors provide absolute assurance or they expect a level of assurance higher than reasonable assurance.³⁵ The deleted language helps explain why these investor preferences and expectations are unrealistic and not attainable.

The Chamber strongly urges the PCAOB to restore the deleted language from AS 1015. Deleting the explanatory language also reinforces our concerns that the Proposal is focused on facilitating PCAOB inspections, regulatory enforcement, and litigation against auditors.

Meaning of the Financial Statements as a Whole

Consistent with the U.S. financial reporting framework, practice has long considered the meaning of “financial statements as a whole” to be just that – the financial statements (including footnotes) taken as a whole. It does not mean an individual line-item of a financial statement, an individual financial statement, or an individual footnote.

Nonetheless, among the many subtle revisions of existing PCAOB auditing standards, without due consideration and economic analysis, is a proposed change in the meaning of the phrase “taken as a whole.” The Proposal includes an amendment to AS 3101 on *The Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion* stating: “‘Taken as a whole’ applies equally to a complete set of financial statements and to an individual financial statement with appropriate disclosures.”³⁶

The Chamber strongly urges the PCAOB to delete this proposed amendment to the meaning of “taken as a whole.” Revising the long-standing meaning of “taken as a whole”

³⁴ See the Exposure Draft, page 27.

³⁵ See the Exposure Draft, pages 39 and 40.

³⁶ See the Exposure Draft, page A4-22.

Ms. Phoebe W. Brown

June 5, 2023

Page 14

represents another example of our concerns that the Proposal undermines the U.S. financial reporting framework and focuses on facilitating PCAOB inspections, regulatory enforcement, and litigation against auditors. And, yet again, by extension, the proposed amendment will impact companies (i.e., issuers and broker-dealers), too, as the meaning of “taken as a whole” applies to all.

Due Professional Care

In consolidating the general principles and responsibilities of the auditor into a single standard (AS 1000), the Proposal eliminates four PCAOB Auditing Standards (AS 1001 on *Responsibilities and Functions of the Independent Auditor*, AS 1005 on *Independence*, AS 1010 on *Training and Proficiency of the Independent Auditor*, and AS 1015 on *Due Professional Care in the Performance of Work*) and significantly revises the provisions of the four standards in the process. The Chamber has concerns about these deletions and proposed revisions.

For example, AS 1000 does not include paragraphs AS 1015.03 and AS 1015.04 that describe the nature of auditor responsibilities for conducting audits with due professional care. This provision has been part of auditing standards for decades. Without this context, investors may be confused about the meaning of due professional care and/or assume the Proposal somehow alters the auditor’s responsibilities in this regard. The Chamber strongly recommends the PCAOB restore AS 1015.03 and AS 1015.04.

Throughout the Proposal, revisions related to auditor compliance with various core principles, including due professional care and professional judgment, tether auditor responsibilities for compliance to the “applicable professional and legal requirements.”³⁷ The Chamber understands that this term is included in the recently proposed quality control standard.³⁸ Nonetheless, we find the term problematic. It lacks clarity – it could mean anything or everything.³⁹

Moreover, the term “applicable professional and legal requirements” appears to exceed the PCAOB’s authority. We note that in accordance with SOX Sections 104 and 105, PCAOB inspection and enforcement investigations assess compliance with SOX, the rules of the Board, rules of the Commission, or professional standards. Professional standards are defined to include auditing, attestation, quality control, ethical, competency, and independence standards as determined by the Board or Commission.⁴⁰

³⁷ For example, see the Exposure Draft, page A1-4 and the professional judgment paragraph on page A1-5.

³⁸ For example, see the Exposure Draft, page 17.

³⁹ For example, narrative (release) text in the Exposure Draft that a reference to professional and legal requirements in the paragraph on professional judgment is not intended to create a new requirement is not particularly helpful. See the Exposure Draft, page 26.

⁴⁰ See SOX Section 2(a)(10)(B). Accounting principles established by FASB or prescribed by the Commission would also be included in the definition of professional standards under SOX Section 2(a)(10). Indications of violations of

The Chamber strongly urges the PCAOB to replace “applicable professional and legal requirements” with a more appropriate term throughout the Proposal. We recommend using the term “PCAOB rules and standards,” which include rules of the Commission and reflect the implement of SOX requirements. “PCAOB rules and standards” define the boundaries of the applicable professional and legal requirements on PCAOB audit engagements.

Professional Skepticism

The Chamber appreciates that exercising due professional care includes exercising professional skepticism in conducting an audit. The current standard, AS 1015.07, defines professional skepticism as “an attitude that includes a questioning mind and critical assessment of audit evidence.” However, the Proposal defines professional skepticism as “an attitude that includes a questioning mind and a critical assessment of information related to the audit.”⁴¹ “Information” is substituted for evidence in other proposed revisions and amendments, too.⁴²

Unfortunately, information (or information related to the audit) is not a defined term in PCAOB Auditing Standards.⁴³ It lacks clarity – it could be anything – especially when viewed after the fact. However, evidence is defined and auditor responsibilities are described in AS 1105 on *Audit Evidence*. Audit evidence is obtained from performing audit procedures. Professional skepticism involves a critical assessment of audit evidence, including objective evaluation of evidence obtained in an audit that supports and corroborates and that contradicts management’s assertions that the financial statements are fairly presented in accordance with U.S. GAAP (or ICFR is effective in accordance with COSO). The Chamber strongly recommends the PCAOB use the term “evidence.”

The Proposal states that the exercise of professional skepticism includes “consideration of potential bias on the part of management and the auditor.”⁴⁴ The phrase “and the auditor” seems added as an afterthought. While the need to consider potential management bias is long recognized, a need to consider auditor bias is new to PCAOB Auditing Standards and introduced into the proposed standard on the auditor’s general responsibilities without explanation or guidance. The Chamber strongly recommends the PCAOB delete it. Rather than improve audit quality, this appears another attempt to facilitate PCAOB inspections and enforcement.

accounting principles affect issuers and the PCAOB has no authority over issuers. However, such indications are reported to the Commission under PCAOB Rule 4004.

⁴¹ See the Exposure Draft, page A1-4 paragraph 1000.10, along with paragraph 1000.11.

⁴² For example, see the Exposure Draft, pages A4-16, A4-30, A4-31, and A4-32.

⁴³ Other standard-setters may use terms such as “information related to the audit.” Even so, this is not PCAOB defined terminology, although narrative (release) text includes a few examples of what the PCAOB considers to be “information.” See the Exposure Draft, page 24.

⁴⁴ See the Exposure Draft, page A1-5.

Professional Judgment

In addition to matters previously discussed related to professional judgment, the Proposal adds a paragraph on professional judgment to AS 1000.⁴⁵ However, the proposed provision does not include language from AS 2815 that “the concept of materiality is inherent in the auditor’s judgments.”⁴⁶ The Chamber strongly recommends that the concept of materiality be included in any provision on professional judgment.

Competence

The Proposal includes provisions related to competence that do not appreciate audits are performed by teams and, therefore, the requirements should apply to teams as a whole.⁴⁷ Although engagement partners have overall responsibility, audits represent the collective effort of an engagement partner, EQR and other partners, professional staff and staff support, specialists, national office consultation staff, and others. In addition, auditors are not lawyers and should not be expected to have expertise in “SEC rules and regulations relevant to the company being audited and the related industry or industries in which it operates.”⁴⁸ As to the latter, while auditors have industry knowledge, they are not industry experts, per se. The auditor’s competence is tethered to financial reporting and auditing related matters. The Chamber recommends the PCAOB recraft these provisions.

Further, proposed amendments to other standards (e.g., AS 1201 on *Supervision of the Audit Engagement*) add requirements for engagement partner responsibilities that are overly prescriptive. In addition, such requirements do not appreciate that the nature of project management and workflow require some flexibility and engagement-specific tailoring for effective audits, including flexibility related to engagement partner review of and sign-off on documentation. Auditing standards should not introduce a “one size fits all” approach. The Chamber strongly recommends that the PCAOB reconsider these provisions from this perspective. As it stands, the amendments appear largely intended to facilitate PCAOB inspection findings and enforcement actions targeted against engagement partners.

Other Matters

The Proposal introduces the notion that relevant guidance includes PCAOB auditing interpretations, Board issued guidance, and releases accompanying the standards and rules of

⁴⁵ See the Exposure Draft, page A1-5.

⁴⁶ See the Exposure Draft, page A1-5 and deleted language on A2-4.

⁴⁷ For example, see the proposed wording of AS 1000.07 in the Exposure Draft, pages A1-6 and A1-7.

⁴⁸ See the Exposure Draft, page A1-3.

Ms. Phoebe W. Brown

June 5, 2023

Page 17

the Board.⁴⁹ As to the latter, it is unrealistic for the Board to designate as authoritative guidance the hundreds of pages of release (narrative) text and the variety of information contained in such text. Commentators may use release text to help understand the rationale and justification for a proposed rule or standard, along with its expected costs and benefits. However, commentators do not comprehensively consider release text in recommending revisions to PCAOB proposals. This point likewise extends to release text in final rules and standards adopted by the Board and subject to SEC due process, with notice and comment as part of the Commission's approval process.

In addition, the Chamber is unaware of any Board issued guidance and it does not appear to be explained or defined in the Proposal. Thus, we do not understand the distinction between rules and standards of the Board versus Board guidance. Importantly, to be authoritative, any Board issued guidance requires due process by both the PCAOB and SEC.

The Chamber strongly recommends that the PCAOB revise the definition of authoritative PCAOB guidance to exclude releases accompanying standards and rules. Any relevant authoritative guidance should be included in a PCAOB rule or standard itself. Further, any (all) PCAOB rules, standards, and guidance intended to be authoritative should be subject to due process by the PCAOB (with public notice and comment) and – after adoption by the Board – submitted to the SEC for approval by the Commission (after public notice and comment).

The Proposal would accelerate the documentation completion date by reducing the maximum time to assemble and complete a final set of audit documentation for retention from 45 days to 14 days from the report release date.⁵⁰ The rationale for this move is to support timelier inspections and provide the strongest incentives for firms to implement operating efficiencies.⁵¹

The Chamber questions whether this revision will have any meaningful impact on PCAOB inspection timelines and operating efficiencies are not the purview of the PCAOB. In addition, we question whether it is workable for smaller audit firms, who may not have the technology to implement this change. We are concerned that it will be another mechanism for generating Part IB deficiencies in audit firm inspection reports and enhancing PCAOB enforcement activities.

Transparency and Due Process

⁴⁹ See footnote 26 in the Exposure Draft, page A1-6, along with page 28.

⁵⁰ See the Exposure Draft, page A3-4.

⁵¹ See the Exposure Draft, page 54.

Ms. Phoebe W. Brown

June 5, 2023

Page 18

The Chamber is a strong advocate for transparency and due process in standard-setting and regulatory rule-making. A basic level of transparency is especially important with this Proposal to understand the nature and scope of the PCAOB's proposed revisions in the general responsibilities of the auditor.

Thus, the Chamber requests the PCAOB disclose those with whom it has consulted on this project. For example, the PCAOB should disclose the name of the former PCAOB chief auditor⁵² and identify any consultants, advisers, or others that have assisted in crafting the Exposure Draft, provided feedback on it in non-public settings (including in non-public meetings of PCAOB advisory groups or committees), or otherwise influenced the development and drafting of it.

Given the nature of this Proposal and the potential for conflicts of interest, transparency is paramount for credibility. To illustrate, individuals or groups that engage in litigation against auditors, or provide expert support for plaintiff attorneys that do, will personally benefit from the Proposal. The Proposal is a dream come true for plaintiffs and plaintiffs' attorneys. The individuals and groups with this type of vested interest in the proposed revisions should not have any influence on the Proposal. If they have had, for this reason alone, the PCAOB should withdraw the Proposal.

Concluding Remarks

In conclusion, the Chamber supports the PCAOB's goal to update its Auditing Standards. Nonetheless, we have deep concerns about this Proposal and strongly urge the PCAOB to withdraw it.

The Chamber also recognizes that setting standards takes time. Due process is essential. We encourage the Board to focus on crafting well informed, balanced, cost-effective standards that will improve audit quality and stand the test of time, rather than simply "rushing to revise" with a focus on enhancing PCAOB inspections and enforcement.

The Chamber hopes that the Board finds our comments and recommendations useful.

Thank you for your consideration and we stand ready to discuss these matters with you further.

Sincerely,

⁵² The Chamber notes that the current Chief Auditor disclosed, at the June 15, 2022 meeting of the PCAOB Standards and Emerging Issues Advisory Group ("SEIAG"), that an (unnamed) former PCAOB chief auditor was assisting her Office with the Board's ambitious standard-setting agenda.

Ms. Phoebe W. Brown

June 5, 2023

Page 19

A handwritten signature in black ink, appearing to read 'TK' with a long horizontal flourish extending to the right.

Tom Quaadman
Executive Vice President
Center for Capital Markets Competitiveness
U.S. Chamber of Commerce