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March 16, 2020

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

Via Email to comments@pcaobus.org

Re: Concept Release, Potential Approach to Revisions to PCAOB Quality Control Standards

Dear Board members:

Grant Thornton LLP appreciates the opportunity to comment on the Public Company Accounting Oversight Board's (PCAOB or Board) Concept Release, *Potential Approach to Revisions to PCAOB Quality Control Standards*. We commend the Board for undertaking considerations to modernize its quality control standards. A firm's system of quality control is a paramount component in maintaining and enhancing audit quality. Given the changes the profession has undergone in the last several years, we agree that it is time for the Board to revise the quality control standards to address such changes in the profession and the advances many firms have made in their systems of quality control over the years. We respectfully submit, for the Board's consideration, our responses and recommendations, including the appendix which specifically addresses certain questions posed in the Concept Release.

Although we acknowledge that the International Auditing and Assurance Standards Board's (IAASB) project on the proposed International Standards on Quality Management (ISQM) is not complete as of the date of this letter, we fully support the Board's approach to using ISQM 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*, as a basis for future PCAOB quality control standards and believe it is essential to closely align the PCAOB standards with ISQM 1. Generally, ISQM 1 provides a principles-based approach to quality control that can provide flexibility and scalability depending on each firm's assessment of risks to its quality control. In addition, we believe there will be great advantages to enabling global network firms to institute one system of quality control. We acknowledge that certain incremental

differences would need to exist due to basic jurisdictional differences, but we caution the PCAOB from incorporating too much prescription into the ISQM 1 requirements due to the wide spectrum of accounting firms that will be impacted by any new standards. The number and significance of the differences between the quality control standards and ISQM 1 could have negative unintended consequences to quality that could ultimately be detrimental to public interest. We encourage the Board to continue to monitor the ISQM 1 project through its conclusion in order to further inform the Board's considerations, as laid out in the Concept Release, prior to proposing a final PCAOB standard.

Nevertheless, we believe the PCAOB has an opportunity to enhance the principles of ISQM 1. We encourage the PCAOB to consider establishing the characteristics of "reasonable assurance" as it relates to firm-level quality control. This is important as the concept of reasonable assurance is not well understood in the context of quality control. Without this understanding, users of auditor's reports, inspectors of audits, and auditors themselves may interpret these standards, as well as the results from the application of these standards, differently, potentially undermining the trust in the audit process itself.

Potential standard-setting approach

We generally support the risk management approach to quality control standards described in the Concept Release, and we believe that the potential revisions described could improve firms' quality control systems. However, while certain aspects of a quality control system are preventive in nature, we believe it would be cost prohibitive for firms to build quality control systems that prevent any and all audit deficiencies. We believe each firm should have the flexibility to adopt an appropriate mix of preventive and detective quality controls for the purpose of providing reasonable, not absolute, assurance regarding the quality control system's effectiveness, similar to the reasonable assurance that auditors obtain in order to render an opinion on a set of financial statements.

Further, we are of the view that additional or alternative requirements for firms that audit brokers and dealers are unnecessary. We believe a system of quality control applies to audit and attest engagements, regardless of industry, and a set of quality control standards that is risk- and principles-based will enable firms to identify industry-specific risks, as appropriate, and respond based on the assessed level of risk.

Firm governance and leadership

We believe that any system of quality control should have a strong foundation of firm governance and leadership. A focus on quality and its importance emanates from the top executives of the firm down to engagement staff, and we support the PCAOB for continuing to view this component as an important aspect of quality control systems. Additionally, we support the ISQM 1 approach to firm governance and leadership and feel that any necessary PCAOB changes to this approach would be minimal.

Supervisory responsibilities

We firmly support robust quality control standards that address the assignment and documentation of supervisory responsibilities at the engagement and firm levels. However, engagement-level supervisory responsibilities differ from those at the firm level. The ultimate responsibility for the supervision and review at the individual engagement level rests with the engagement team – in particular, the engagement partner. Supervisory responsibilities at the firm level relate primarily to monitoring the operation of a firm’s system of quality control as a whole and address, among other things, managing firm operations, providing technical and specialty support, and procuring and managing personnel and technology resources. Firm-level supervisory deficiencies ordinarily pertain to a failure in the system of quality control to either prevent or detect such deficiencies, but often do not directly link to a deficiency in a particular engagement. It is not possible for firm-level personnel to directly supervise all, or portions of, each individual audit engagement.

Inappropriate emphasis may be placed on assigning individuals in specific areas of supervisory responsibility, in lieu of viewing supervision and monitoring as a collective effort involving several individuals and related firm processes. An unintended consequence of requiring a more prescriptive approach that overemphasizes the role of an individual as opposed to the firm’s quality control processes is that it could affect an individual’s perceived ability and initiative to consider and address supervisory matters outside of the individual’s specific area of assignment. Firms may also be exposed to undue harm in the form of sanctions, loss of registration, or other reputational risk if the Board were to take enforcement action for a predicate violation against firm-level supervisory personnel by focusing solely on the individual’s responsibilities, without considering the firm’s system of quality control as a whole. We believe that such consequences may result in diminished audit quality. Therefore, we support the proposed requirements of ISQM 1 and strongly encourage the Board to be cautious in adopting incremental requirements in future rulemaking.

Independent oversight

We are supportive of the notion that independent directors or advisory committees can provide helpful business insights to audit firms. However, we believe that adopting specific requirements in this area could create considerable operational challenges, depending on a firm’s governance structure, the size of the firm, and various other aspects (for example, the nature of the audit or attest engagements performed). It is also unclear how an independent member of the firm’s board would directly impact or oversee a firm’s system of quality control, and we are concerned about whether the cost/benefit of such requirements would be scalable.

We also note that a significant challenge to adopting such requirements relates to a director being independent not only of the firm, but also independent of all the firm’s clients, given the director likely would be viewed as part of the “chain of command” related to the firm’s system of quality control. In addition, we are concerned that charging such independent director with overseeing audit quality could create a potential liability that otherwise qualified individuals may find untenable.

We believe that a similar objective can be met by either designating an individual on a firm's board as an "audit quality expert" (similar to audit committee requirements for a "financial expert") or by having independent external advisors outside of the board construct, to focus on and advise firms regarding audit quality or their systems of quality control.

Regardless of the path the Board chooses, we do not believe specific criteria should be used to determine which firms would be required to have independent oversight. If the Board believes that audit quality will be enhanced by such oversight, we do not believe certain firms should be exempt from such requirements. Rather, we encourage the Board to establish requirements that can be appropriately instituted by all registered firms, considering the operational challenges we noted above.

Financial resources

While we appreciate the nature of the contemplated requirement related to appropriate allocation of firm financial resources, it could be difficult to determine what constitutes "sufficient" and how that would be measured and monitored by the firm and regulatory bodies. Additionally, we believe investments in firms' other complementary services, such as tax or advisory practices, are essential to audit quality. Therefore, categorizing such investments to support a financial resources investment target may be difficult to measure and apply. Therefore, we support the approach proposed by ISQM 1 and do not believe incremental or more specific requirements are necessary.

The firm's risk assessment process

As with planning an audit, we believe that an appropriate risk assessment process provides an appropriate path forward in executing an effective system of quality control. We believe principles-based requirements would be sufficient to meet the objective of this component of a quality control standard. We note that proposed ISQM 1 provides considerable application guidance and helpful considerations to guide firms. The risk assessment process will be unique to each firm based on their size, client base, and other circumstances. Therefore, we encourage the Board to develop similar guidance such that firms can effectively develop and maintain an appropriately robust risk assessment process without embedding specificity into the requirements.

We would not be opposed to specific quality risks, but we believe such risks should be both relevant and significant, to a firm's quality control processes in order to merit specific requirements. We analogize to the presumed risk of fraud in revenue recognition that is currently required in the auditing standards. We further note that such presumption can be overcome; therefore, we would expect that any presumed quality risks written into the quality control standards could also be overcome under certain circumstances. We do not believe adopting specific quality risks within the quality control standards should be driven by, for example, recent inspection findings or other "hot topics" that may become less relevant over time.

Relevant ethical requirements

We support the proposed approach to the ethical requirements component of systems of quality control. We believe that adhering to relevant ethical requirements, including independence requirements, is another foundational concept that not only promotes audit quality but also safeguards the vital role auditors play within the capital markets. In addition, we support the potential differences from ISQM 1 that are laid out in the Concept Release. Specifically, we support expanding the applicability of what are currently SEC Practice Section (SECPS) requirements to all firms. Firms that are currently subject to the SECPS requirements have likely invested considerable capital and resources to implement and maintain the tools that enable compliance with the SECPS requirements. We view that investment as worthwhile and believe these requirements have contributed to audit quality over the years and therefore could benefit all registered firms.

However, we agree that certain refinements may be necessary in order to more broadly apply the requirements and not to create undue financial hardship on firms. For example, the Board may reevaluate the threshold of “more than 500 SEC registrants,” in order to ensure that any costs that would be incurred to implement an automated system make fiscal sense for firms (that is, a firm with many SEC registered clients but only a small team of personnel may identify this as a risk and establish appropriate safeguards, which may or may not be an automated system).

Further, we generally support the updates and refinements described on page 21 of the Concept Release. However, we are of the view that engagement-level, not firm-level, quality controls are most relevant to responsibilities for communications with audit committees regarding independence matters. While firms’ national offices may provide the tools and guidance to engagement teams to enable them to provide the appropriate information pursuant to PCAOB Rules 3524, 3525, and 3526, it is ultimately the engagement team’s, in particular the engagement partner’s, responsibility to determine that such communications are conducted. It would not be feasible from a cost/benefit perspective to establish firm-level controls over the engagement-level execution of these communications for all engagement circumstances. We encourage the Board to be clear in this regard in any future proposed rulemaking and to consider whether current practice and inspection results would necessitate enhanced requirements.

Acceptance and continuance

As a key component of a firm’s quality control, we support robust processes and controls around client and engagement acceptance and continuance. We agree with the Board’s initial expectation that changes would not fundamentally alter a firm’s existing responsibilities regarding acceptance and continuance decision-making. We caution the Board against adopting specific requirements, at the firm quality control level. Specifically, regarding situations where the firm becomes aware of relevant contrary information after the initial acceptance or continuance decision. We believe that ongoing evaluation of acceptance or continuance occurs at the engagement level by the engagement partner and that any firm-level controls in this area would be more appropriately based on a firm’s identified and assessed risks as opposed to a specific

rules-based requirement. We also note that monitoring engagement performance from an audit quality perspective is better suited to identify recommended changes to the firm's overall client acceptance process when quality issues are noted to be more pervasive.

Engagement performance

We support aligning any future quality control standards with relevant auditing standards, such as supervision, document retention, and engagement quality review. In that regard, we believe that the concepts currently captured in QC 20, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice*, would continue to be applicable and that the requirement is written in such a manner that enables firms to adjust quality processes and controls, depending on the extent to which they use parties outside the firm. We would support the Board in clarifying the language of extant QC 20 to indicate that the requirement is applicable to non-affiliated firms, auditor-engaged specialists, and service delivery centers that are not already subject to the US firm's system of quality control. However, prescriptive requirements beyond such clarifying language could be difficult to operationalize, particularly since many of the items under consideration are already expressly addressed in the PCAOB auditing standards. It is unclear how another layer of controls, at the quality control level, would enhance audit quality without introducing untenable costs into the system.

Resources

Technology

The proposed requirements of ISQM 1 incorporate not just personnel resources but also technological resources. We recognize firms are at different places relative to how and the extent to which technology is integrated into their audit methodologies. Nevertheless, we support this expansion and believe a principles-based set of requirements, similar to that provided in proposed ISQM 1, will enable firms to tailor their risk assessment and response based on the extent to which firms use different technologies. It is unclear to us, however, whether specifically requiring firms to maintain controls that prevent unauthorized access to technology and related data is intended to address a business risk to the firm or a risk to audit quality. Further, we are concerned that any prescription in the quality control standards could differ from data privacy and use laws and regulations that are established by other regulatory bodies with which firms must comply. This could put firms in a difficult position unless the risk is associated directly with undermining the firm's infrastructure for obtaining sufficient appropriate audit evidence. We believe the proposed ISQM requirements would enable firms to identify what, if any, access-related risks exist in the context of audit quality and to respond accordingly based on the assessed level of risk. We encourage the Board to remain principles-based and focused on the objective of audit quality when considering incremental requirements in this area.

If the Board decides to address emerging technologies in the quality control standards, a principles-based approach should appropriately capture the topic such that firms can identify their individual risks and the related responses. We are of the view that the extent to which firms address emerging technologies will depend on the

extent of their use and whether they directly link to obtaining sufficient appropriate audit evidence.

Technical training

Continuing education plays an important role in firm professionals maintaining sufficient competencies to fulfill their job responsibilities. We believe the existing requirements related to CPE hours and subjects is sufficient and provides firms with enough flexibility to identify the training needs specific to their audit practices. We are concerned that more prescriptive requirements could increase the risk of training being overly focused on compliance as opposed to using appropriate methods to build the knowledge and skills that are relevant to the needs of engagement personnel. We agree that, for example, annual training on professional standards is important. We call attention to the PCAOB's "Critical Audit Matters Spotlight" where the PCAOB staff observed that firms "made significant investments in developing methodologies, tools, and training...these investments appear to have made important contributions to support the firms' implementation efforts."¹ We believe the observations from the critical audit matters implementation demonstrates firms' abilities to use principles-based standards (that is, the existing quality control standards) to identify the appropriate areas where training investments are necessary.

Professional competencies

We support retaining and updating existing requirements regarding engagement partner and engagement quality reviewer competencies. We believe the additional competencies described in the Concept Release are reasonable and appropriate. We do ask the Board to consider clarifying the competency related to understanding technology used in obtaining and evaluating audit evidence. We assume the Board intends for this understanding to be in the context of an engagement partner's ability to use firm technology as intended. This level of understanding is quite different from understanding the inner workings of all technologies and the national-level processes that are undertaken to develop and maintain such technology. By clarifying the extent of understanding, the Board could establish a requirement that is more operational for audit firms.

With regard to other personnel in engagement roles, we do not disagree with the Board's observation that appropriate competencies may be particularly important to some roles other than engagement partner and engagement quality reviewer. However, under a principles-based set of quality control standards, firms would be able to appropriately identify those particular roles within their firm structure and address them accordingly within their system of quality control.

While contemplating the Board's observations related to competencies, we question whether the idea of a single engagement partner taking responsibility for the entire audit is becoming antiquated and possibly unrealistic and whether the PCAOB has considered this concept in regard to competency as discussed in the Concept Release. As audits become more complex, we believe it is a significant, collective

¹ "Critical Audit Matters Spotlight," Public Company Accounting Oversight Board, December 10, 2019.

effort that brings all appropriate skills to the engagement team to gather audit evidence and conclude on the appropriateness of the financial statements, disclosures, and, when applicable, whether internal control over financial reporting (ICFR) is effective. We wonder whether it is practical to continue to believe that a single engagement partner can sufficiently possess all the necessary skills. We ask the Board to consider whether engagement partners are becoming more like general contractors in a building project: they may not be an expert in all the areas involved in building a house, but they know what is necessary to build the house and how to involve appropriate experts. As the Board considers the requirements related to competencies, we encourage the Board to consider how a different supervisory structure may improve overall audit quality, recognizing that such a change would require other revisions to PCAOB standards, rules, and forms.

Information and communication

We generally support the proposed requirements of ISQM 1, and it is unclear why the PCAOB may believe it is necessary to include requirements related to communications with audit committees, the SEC, or others when ISQM 1 includes a requirement related to communications with external parties in accordance with laws, regulations, or professional standards. We believe that would sufficiently address the specific communication requirements audit firms have here in the United States. We also believe that a certain level of flexibility is necessary as it relates to this component of a system of quality control, particularly because information and communication processes are often embedded in quality processes under other components. Otherwise, we support the Board's contemplated approach to this component of a firm's system of quality control.

Additionally, we are supportive of a certain level of public disclosure regarding firms' systems of quality control. We note that in the PCAOB's "Conversations with Audit Committees" publication, the PCAOB observed that "most audit committee chairs evaluated audit quality with an emphasis on their engagement team, with a lesser degree of focus on the characteristics of the audit firm."² Therefore, we believe there is a fine line between disclosure that is informative and beneficial versus disclosure that may not provide meaningful information.

By way of example, we support disclosures like those that many firms make currently in their annual transparency reports. We believe describing certain aspects of firms' systems of quality control could be informative and useful to relevant stakeholders. However, for certain firms, the cost and effort that would be focused on public reporting could very well detract from the effort to ensure that the system of quality control is operating effectively. Further, we believe that any public statement on the effectiveness of a firm's system of quality control could be extremely confusing because general stakeholders would not have the appropriate context to interpret what such a conclusion means to them. If the Board proceeds with requiring public disclosures, we urge the Board to focus on aspects of a firm's system of quality control and to avoid requiring public disclosure of conclusions or statements regarding

² "Conversations with Audit Committee Chairs: What We Heard & FAQs," Public Company Accounting Oversight Board, December 18, 2019.

the effectiveness of the firm's system of quality control. Refer to additional comments on external reporting in the "Monitoring and remediation" section below.

Monitoring and remediation

Monitoring

We support requiring a mix of proactive and detective monitoring activities that allows firms to determine the appropriate firm- and engagement-level processes based on the firm's risk assessment. We believe many firms have adopted processes such as these already. As such, we agree that ongoing monitoring activities could be beneficial in the timely identification of potential quality issues; however, such activities can be time consuming and costly to maintain, which is why we believe a principles-based approach that allows for a risk-based response by firms would be the most beneficial to firms' audit quality while allowing for appropriate scalability.

We are concerned with the general level of prescription being considered by the PCAOB in this area. We believe that driving specific requirements into monitoring activities would be cost prohibitive and could become "check the box" exercises as opposed to being responsive to the identified risks. For example, we are of the view that root cause analysis is a potential response to an identified risk in audit quality. Therefore, expressly requiring root cause analysis to be performed assumes that all firms have the same risk and that the appropriate response is to perform root cause analysis. Root cause may be an appropriate response for particular firms, but for others it may overcomplicate the firm's process and might not necessarily be an efficient response to the assessed level of risk.

We are not opposed to aligning quality control requirements more closely with AS 2901, *Consideration of Omitted Procedures After the Report Date*, and AS 2905, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*. We believe evaluating internal and external inspections findings and monitoring any resulting remedial actions is important. However, because the severity of inspection findings can vary significantly, we believe any monitoring activities required by the standard should be flexible enough so that they can be risk-based.

Evaluation and reporting

We support the proposed requirement of ISQM 1 to make an assessment, at least annually, of the effectiveness of a firm's system of quality control. We further support the PCAOB's expectation that the firm has a reasonable basis for its conclusion (refer to the "Documentation" section below for more specific views on that aspect). However, we struggle to understand the purpose of providing annual reports on quality control to the PCAOB. All quality control-related documentation and conclusions would be available and subject to PCAOB inspection. Therefore, preparing a formal report to be submitted to the PCAOB in addition to the inspections process appears unnecessarily duplicative. We ask the Board to move forward with the requirements as proposed in ISQM 1 and not to require incremental reporting.

As alluded to in the "Information and communication" section above, we have significant concerns with any public reporting or certification by firm leadership regarding a conclusion on the effectiveness of the firm's system of quality controls.

We have two main concerns with public certifications or conclusions on quality control effectiveness: (1) analogizing to management's assessment of ICFR is inappropriate since the subject matters and the context in which they are evaluated are very different; and (2) firm conclusions with regard to identified deficiencies and quality control effectiveness would be vastly misunderstood by external stakeholders when considered in the context of other publicly available information.

Management's assessment of ICFR is most often performed under the COSO framework, which is a long-established framework. Currently, users of financial statements can consider the COSO framework in evaluating management's and the auditor's reports on the effectiveness of a company's ICFR, and there is a direct link between ICFR and the related financial statements. In contrast, systems of quality control, as noted above, are dynamic and do not have an "anchor" such as the financial statements. Notwithstanding an issue in a firm's system of quality control, the audits performed by the firm may comply with PCAOB rules and standards because the procedures performed capture sufficient appropriate audit evidence. In contrast to an ICFR report by management that states, notwithstanding an identified material weakness in ICFR, that the financial statements are not materially misstated, there is no balancing opinion to indicate that the audit reports issued by the firm are still reliable. Thus, a publicly reported quality control certification that indicated a problem would undermine all the audits of the firm and create undue pressures for firms to misreport the overall conclusion on its system of quality control. Therefore, we believe any conclusion on the effectiveness would lack appropriate context for individuals outside audit firms and the PCAOB.

In addition, there is currently no framework for evaluating deficiencies in quality control or the effectiveness of the system of quality control itself. We believe the Board needs to address questions such as the following: *What does effective quality control mean?*, *How should findings or deficiencies be evaluated?*, and *How do they affect the overall conclusion related to quality control effectiveness?* A firm's system of quality control does not and cannot efficiently function if the objective or assumption for effectiveness is "zero defects." Therefore, a framework is critical for firms to appropriately, and consistently, assess the effectiveness of their systems of quality control. The current inspection program further complicates the ability of a firm to provide an overall conclusion on its quality control effectiveness since there is a requirement to identify the element of the quality control system that failed to cause the inspection finding. This suggests that a single inspection finding renders the quality control system ineffective.

We also believe that any conclusions provided by an audit firm regarding quality control effectiveness could be impacted if part or all of a firm's non-public inspection report (Part II) is made public. We note that there may be a considerable time lag between when the firm is required to conclude on effectiveness and when an inspection report is made public. We are concerned that those quality issues could be misconstrued and viewed as contradicting the firm's previous conclusion that the system of quality control is effective. It could be extremely challenging for stakeholders to understand and reconcile the information that would be publicly available under the requirements contemplated in the Concept Release, especially

given the considerable time period between the issuance of firm public reports and the release of non-public firm inspection findings.

Documentation

Generally, we support the proposed requirements in ISQM 1 regarding documentation. We believe they are appropriately principles-based and therefore encourage the PCAOB to adopt the requirements with minimal incremental changes. We have considerable concerns over the incremental or alternative requirements that the PCAOB is considering. The documentation efforts our firm has undertaken to prepare for adopting ISQM 1 have been and will continue to be a significant investment, both in time and cost. While we believe it a worthwhile investment, firms will reach a point of diminishing returns if too much prescription is embedded in the quality control standards, which is why we are in favor of the ISQM 1 proposed requirements.

We believe a document retention period of seven years is overly burdensome. The ISQM 1 approach appears more operational and enables firms to establish retention periods that make practical sense, notwithstanding retention periods governed by laws and regulations. Because systems of quality control are dynamic, process memos and controls documentation would be “live” documents that are maintained with “as of” dates as opposed to audit workpapers that are archived once the auditor’s opinion is rendered. We further note that any documentation, such as documentation regarding consultations that the PCAOB refers to on page 41 of the Concept Release, would be retained in the applicable audit workpapers. Given the nature of a firm’s system of quality control, we do not believe a retention period similar to the audit workpaper retention period is necessary. Therefore, we envision, and encourage the PCAOB to consider, that documentation need only be retained through the time period during which a firm makes its annual assessment and the PCAOB inspects that assessment, either within the year or within the triennial period, unless law or regulation requires a longer retention period.

Roles and responsibilities

We fully agree with establishing requirements for the individuals assigned ultimate responsibility and accountability for the system of quality control and operational responsibility for monitoring and remediation, as proposed by ISQM 1. We believe such requirements complement those proposed by ISQM 1 related to firm governance and leadership. We further support the PCAOB’s consideration of adding requirements related to the individual(s) responsible for independence quality controls. As noted in our comments above, independence is of paramount importance, and we believe the responsibilities enumerated on page 43 of the Concept Release would be appropriate to include in the quality control standards.

However, we have significant concern with attributing such responsibilities to “all firm personnel.” We believe this categorization is overly broad and could create operational challenges for firms. In particular, the use of “all” implies any employee of the firm, regardless of whether they participate in audit or attestation engagements, for example, administrative assistants, marketing personnel, and others. We encourage the Board to refine the scope of individuals to whom these responsibilities

would apply that would reflect what we believe the Board intends, such as “all engagement personnel.” We believe these responsibilities would be appropriate to include in the quality control standards, and they would be best suited to a narrower group of individuals that is more in line with the other standards and rules of the PCAOB.

Related potential changes to other PCAOB standards

Generally, we are in favor of the changes to AS 2901 that the Board discusses in the Concept Release. We agree that the fundamental responsibilities should not change, but that better clarifying the requirements could enhance auditors’ understanding and appropriate application of the standard. We also support any changes being reflected in AT 1, *Examination Engagements Regarding Compliance Reports of Brokers and Dealers*, and AT 2, *Review Engagements Regarding Exemption Reports of Brokers and Dealers*, as appropriate.

We recognize that AS 1110, *Relationship of Auditing Standards to Quality Control Standards*, is repetitive with requirements in other standards, but we believe that AS 1110.03 remains quite relevant and disagree with the Board’s concern related to auditors misunderstanding its meaning. Considering the Board’s project to revise the quality control standards, this paragraph provides an important fundamental distinction in the relationship between engagement performance and a firm’s system of quality control. While we acknowledge that deficiencies in firm quality control increase the risk of individual audits having audit deficiencies, it is not and cannot be a foregone conclusion that audit deficiencies will exist at the engagement level for all engagements. We analogize to financial reporting where there are many situations when an auditor issues an adverse opinion on ICFR reporting, but no adjustments to the financial statements result from the material weakness(es) in order for those financial statements to be in accordance with the applicable financial reporting framework in all material respects. We are concerned that by rescinding AS 1110 and effectively removing AS 1110.03, the Board could inappropriately imply that any deficiencies in firm quality control could result in a conclusion that no individual audit engagement was performed in accordance with the auditing standards.

Scalability

We believe that too much prescription could stifle firms’ ability to apply a risk-based approach to developing and maintaining their systems of quality control. Conversely, we believe too much scalability creates different levels of quality and execution and potentially a false sense of protection for investors. Therefore, we encourage the Board to develop principles-based standards that are risk-based, which would enable firms to consider factors such as the complexity of the firm and the nature of the firms’ engagements and to respond appropriately based on the relevant risks associated with such factors. We believe exempting firms from certain requirements simply due to their size, complexity, or client base could do a disservice to the profession and negatively impact overall audit quality.

We also feel that due to the volume of application material that is included in proposed ISQM 1, registered firms that do not otherwise have to comply with international standards would benefit from guidance from the PCAOB on how the



ISQM 1 application material could be considered in the context of the PCAOB quality control standards.

We would be pleased to discuss our comments with you. If you have any questions, please contact Bert Fox, National Managing Partner of Professional Standards, at (312) 602-9080 or Bert.Fox@us.gt.com.

Sincerely,

/s/ Grant Thornton LLP

Appendix

Responses to selected Concept Release questions

Following please find our specific responses to certain of the questions posed in the Concept Release that are not addressed in the body of our letter or are included to further expand on the discussion above.

Question 5: To the extent that audit firms are already updating or making enhancements to their QC systems to align with international developments, can you characterize the nature and extent of those changes and related efforts? What benefits do you anticipate from updates to QC systems?

Many processes have evolved, and focusing on what and why each process exists in terms of contributing to overall audit quality continues to be a positive evolution. Given the substantial investment in resources and lead time necessary to adopt the standards, our global network and, to a certain extent, some of the member firms, have begun implementing processes to adopt firm updates and enhancements initially focusing on those areas most affecting audit quality.

We believe global firms will benefit from a consistent response related to quality control requirements. Therefore, it could be costly for member firms in jurisdictions that adopt ISQM 1 to incrementally monitor or adopt quality control processes that adhere to any PCAOB US-specific differences.

Question 8: Would the objective of a quality management system provided in Proposed ISQM 1 be an appropriate objective for a QC system under PCAOB standards? Are there additional objectives that a quality control system should achieve?

We believe the proposed objective for ISQM 1 would be appropriate for QC systems under PCAOB standards, and we do not propose any additional objectives.

Question 10: Would the potential revisions to PCAOB QC standards described in this concept release enhance firms' ability to prevent audit deficiencies? Are there additional revisions to PCAOB QC standards that we should consider to support a preventive approach to managing quality?

Overall, we believe the potential revisions would enhance audit quality. With respect to audit deficiencies, we believe this depends on how "audit deficiencies" are defined

by the PCAOB in the new standards. We do not expect that firms will be achieving “zero defects,” as it would be impossible for a set of standards to set out such an objective. So, while we do expect findings during inspections to continue to occur, we note that firms will require further guidance on those rising to the level of a deficiency, including how a firm would consider compensating controls and aggregation criteria. We believe this area will be an important one for developing implementation guidance and conducting outreach to hopefully drive consistency in how firms evaluate and conclude on deficiencies.

Question 11: Should a future PCAOB QC standard have additional or alternative requirements for firms that audit brokers and dealers? If so, what?

No, we do not believe there should be additional or alternative requirements for firms that audit brokers and dealers. Instead, we believe a principles-based set of standards would enable firms to address any unique aspects firms may identify related to the quality of audits of brokers and dealers. We have noted in our overall comments areas where additional requirements or prescription may result in additional costs without commensurate benefit for all auditors, including those who audit brokers and dealers. We believe focusing on scalability, as the PCAOB has noted, will be of critical importance, as opposed to developing specific requirements for certain engagement types.

Question 12: What would be the costs and benefits of implementing and maintaining an integrated QC system as described in this concept release? Are there particular costs and benefits associated with specific components that we should consider? What, if any, unintended consequences would there be?

Although we believe that enhancing the quality control standards using a risk-based approach is important, more formal and prescriptive processes, including the testing of operating effectiveness of quality controls and the contemplated level of documentation and reporting, would be very costly to implement and maintain. We ask the Board to consider such costs in the context that no efficiencies are gained at the engagement level for firm-level quality controls, so that such costs would be incremental to the costs firms already incur to deliver services to their clients. The Board may wish to address during its standard-setting process that new quality control standards would likely increase the overall cost of audit services to issuers.

Question 18: Is the approach to the firm’s risk assessment process appropriate (i.e., use of ISQM 1 requirements as a starting point, with incremental or alternative requirements)? Are changes to the approach necessary for this component?

With regard to the risk assessment component, we encourage the Board to provide flexibility and remain principles-based in the requirements. Since this is a new area for firms to be formalizing and documenting, we believe it will take time to determine the best and most appropriate approach to complying with the applicable requirements.

Question 19: Are principles-based requirements sufficient to prompt firms to appropriately identify, assess, and respond to risks, or is supplemental

direction needed? If supplemental direction is needed, what requirements would assist firms in identifying, assessing, and responding to risks?

We believe that principles-based requirements are sufficient for firms to appropriately execute such requirements. Supplemental direction by way of guidance is always beneficial to firms. For example, we believe firms benefited greatly from the various pieces of guidance the PCAOB staff provided before the requirements for critical audit matters became effective. We encourage the Board to consider avenues for guidance whereby the requirements can remain principles-based, but the Board can provide direction in particular areas or aspects of the standards, if necessary.

Question 21: Should firms be required to establish quantifiable performance measures for the achievement of quality objectives? If so, how should such measures be determined and quantified (see also Question 46)?

We believe that the profession continues to try to identify quantifiable performance measures that could be meaningful or correlate to audit quality. We note one of the working groups established by the International Forum of Independent Audit Regulators is endeavoring to determine appropriate recommendations for defining a framework of audit quality indicators. While we support the notion that quantifiable measurements will be important for some quality objectives, we suggest that the requirements not go beyond the precision that the nature of the subject matter allows. Therefore, we would not recommend that the Board establish such measures in the quality control standards and instead allow firms to determine the appropriate measures of their quality objectives, possibly over time as firms adopt the risk-based approach to quality control.

Question 26: Should PCAOB QC standards be revised to address developments in audit practices and provide more definitive direction regarding firm QC systems? Are there other reasons for changes to the QC standards that we should take into account?

We encourage requirements that are principles-based; we believe considering developments in the audit and attest landscape would be a key element of firms' risk assessment. We believe that certain topics or developments could also be addressed through audit standard setting, as evidenced by the enhancements to the auditor's application of professional skepticism in the PCAOB's new standard on auditing accounting estimates.

Question 27: Should a future PCAOB QC standard expressly address the use of other audit participants? If so, should the scope of the requirements include affiliated and non-affiliated entities and individuals, including specialists and service delivery centers? Should we consider any changes to the scope of the potential requirements described? If so, what changes would be necessary?

We believe it could be beneficial for future standards to address the use of other audit participants; however, in order for firms to reap those benefits, the requirements should be principles-based and focus on the firm's identification of the related risks in using those other participants and in subsequently developing appropriate quality objectives and responses, rather than prescribing specific actions or requirements.

While a firm's system of quality control could contemplate institutional use of other audit participants, it may be difficult and cost prohibitive to anticipate, assess, and monitor at the firm level those participants involved in the audit engagement, particularly those with limited involvement. Therefore, we believe the auditing standards are best to govern the specifics of using other audit participants. For example, the limited use of a correspondent firm in a jurisdiction to observe a particular physical inventory would not likely require firm-level evaluation. Rather, the engagement team would determine the extent of vetting of competence and supervision over that correspondent firm. We note the importance of allowing firms flexibility in determining the appropriate quality control processes at the firm level and encourage the Board to focus the requirements on firms developing responses to identified risks.

Question 28: Should the Appendix K requirements be retained? Should the scope or application of the Appendix K requirements be changed, for example, to extend the requirements to all audits in which a non-U.S. firm issues an audit report on the financial statements of an issuer, or to exempt certain audits from one or more requirements? Should the individual requirements in Appendix K for filing reviews, inspection procedures, or disagreements be revised or updated? If so, how? Is it clear how the responsibilities of an Appendix K reviewer differ from the role of the engagement quality reviewer?

We agree with the PCAOB's observations regarding the evolution of reporting for foreign private issuers and related Appendix K requirements. We believe that Appendix K was designed to obtain assistance from global firm networks to enhance the quality of SEC filings for foreign member firms. Appendix K describes the procedures the individuals with expertise in US financial reporting and auditing rules within these networks (reviewer) are required to perform; we note that most of those procedures are inquiries. We believe there is still merit and benefit to Appendix K reviews, and we would support retaining the requirements, with any changes limited to those necessary to reflect the changing landscape described in the Concept Release. We believe the focus on the "form of the filing" continues to be most relevant from a reviewer's perspective. Additionally, although we recognize that the likelihood of a deficiency being identified during an Appendix K review may not be as prevalent as it once was, we believe the process does enhance the quality of financial reporting.

We do not support expanding the scope of Appendix K reviews and believe any updates to the standard should retain the clear separation of the reviewer from the engagement team, including the engagement quality reviewer. Therefore, we support retaining Appendix K requirements substantially as is.

Question 30: How should a future PCAOB QC standard expressly address firms' actions to support the fulfillment of the auditor's responsibilities under Section 10A of the Exchange Act, including:

- a. With respect to fraud?
- b. With respect to other illegal acts?
- c. With respect to going concern consideration?

We believe firms' actions related to the auditor's responsibilities under Section 10A of the Exchange Act are most appropriately handled through the auditing standards associated with the topics listed above. We do not believe incremental, prescriptive requirements at the firm level are necessary because proposed ISQM 1 would incorporate firms' consideration of legal or regulatory obligations in their jurisdiction as part of risk assessment. Firms then could develop responses that are appropriately responsive to the risks identified.

Question 37: Should a future PCAOB QC standard expressly address how the firm's incentive system, including compensation, incorporates quality considerations? If so, how?

We would support principles-based requirements for incorporating quality considerations into firms' incentive systems. Nevertheless, we are of the view that an incentive system is most successful if it balances personal, profession, and quality matters. Overemphasis, or absolute focus, on quality could have a long-term adverse effect on quality because it could deter high-caliber individuals from joining the profession.

Question 43: Should all firms, as part of their monitoring procedures, be required to have internal inspections of their completed engagements? If not, which firms should not be required to have inspections of their completed engagements, and what alternative measures should be required for those firms?

In general, we believe that some form of an internal inspection program is best practice for conducting objective evaluations of firms' audit quality and compliance with the applicable auditing standards. We would support a requirement that allows the firm to determine the nature, timing, and extent of its internal inspection program, in addition to any PCAOB inspections to which firms are subject (also see response to Question 44).

Question 44: Should a future PCAOB QC standard establish requirements for internal inspection selection criteria? Should a future PCAOB QC standard specify minimum or cyclical thresholds for inspections of completed engagements by the firm? If so, what should the threshold(s) be (e.g., one engagement for each engagement partner, and/or the audit of each issuer, broker, and dealer on a specified basis)? Should we require selection of engagements for internal inspection to include either random selection or an element of unpredictability?

While we believe that all firms should have a process in place for evaluating or monitoring audit quality, we do not agree with the future quality control standards dictating specific requirements, such as selection criteria, minimum thresholds, and others. We believe that internal inspection programs should be responsive to a firm's risks. This is another area where we recommend the Board consider providing guidance or examples of "best practices" outside of the quality control standards themselves.

Question 50: Should we require firms to document their understanding of network or third party provided methodology and tools, including how such methodology and tools are responsive to the requirements of the professional standards and applicable legal and regulatory requirements?

We agree that in order to achieve high quality, firms cannot place undue reliance on methodology and tools provided by the network. Nevertheless, we are concerned with the specificity and extent of the Board's potential incremental or additional requirements in this area. Individual firms should be responsible for their own system of quality control; however, a network shares the same reputation as the firms within the network and has a vested interest in promoting quality among the individual member firms. Arguably, the risks to quality are more extensive at firms that do not have access to the extensive resources a network can provide, and we are concerned that any incremental requirements could place a larger burden on firms that participate in the benefit of these resources.

We believe that any risks resulting from network tools and resources would be identified through firms' risk assessment processes and would not require express requirements. Principles-based requirements would enable firms to identify and respond appropriately based on the assessed level of risk that may exist with respect to network resources.

Question 55: Are there other PCAOB standards for which substantive changes might be needed to align with a future PCAOB QC standard?

We believe that undertaking the project to revise the quality control standards highlights the need for enhancements to the auditing standards currently under consideration in the Board's project on the supervision of audits involving other auditors. Enhanced requirements related to supervising other auditors would greatly benefit audit quality and would complement firm-level quality controls contemplated in the Concept Release.

We also recommend the Board consider AS 1301, *Communications with Audit Committees*. While we don't foresee substantive changes, this standard may benefit from a reassessment after the quality control standards are finalized.

Question 57: Are there aspects of the approach described in this concept release that would disproportionately affect smaller firms? If so, which areas, and what steps could the PCAOB consider to mitigate those effects?

We believe the potential incremental requirements considered by the Board in the Concept Release in the information and communication, monitoring, and documentation components may not meet the scalability objective set out in the Concept Release and therefore could disproportionately affect smaller firms. As noted in a number of areas in the body of our letter, these effects could largely be mitigated by remaining principles-based and minimizing the number of incremental requirements to proposed ISQM 1.