March 16, 2020

Via email: comments@pcaobus.org

Public Company Accounting Oversight Board
Attn: Office of the Secretary
1666 K Street NW
Washington, D.C. 20006-2803


To the Board Members and Staff of the
Public Company Accounting Oversight Board (PCAOB):

BDO USA, LLP welcomes this opportunity to comment on the PCAOB’s Concept Release on the Potential Approach to Revisions to PCAOB Quality Control Standards. We believe that a firm’s system of quality control is quintessential to a firm’s ability to provide quality audits; therefore, we support the PCAOB’s efforts to revise the PCAOB’s Quality Control Standards. These standards were originally developed by the AICPA and subsequently adopted by the PCAOB in 2003. With significant advances in technology and management practices, many firms’ systems of quality control have evolved since the development of these existing standards.

Further, consistency in design and application of quality control standards across firms domestically and internationally is imperative for corporate and government entities, firms, and the investing community to rely on and compare quality across firms.

In addition to providing responses to the 58 questions posed in the request for comment, we have provided certain macro considerations that we are asking the PCAOB to evaluate.

Overall Comments

Comment #1: Principles-based, risk-based approach

We support the PCAOB’s efforts to base a new standard on the International Auditing and Assurance Standards Board’s (IAASB) proposed International Standard on Quality Management 1 (ISQM 1) as proactive and effective Systems of Quality Control are fundamental for firms to provide consistent, high-quality audits. This proposed standard incorporates governance and leadership, risk assessment, and information and communication as new quality control components and takes a proactive approach to managing quality.

We believe a principles-based, risk-based approach that is aligned with ISQM 1 will enable firms to design and implement a system of quality control to address the risks inherent in each firm. We further believe that such an approach will allow for the standards to not only reflect the current auditing environment but also be adaptable to future changes within the auditing profession. Such
an approach will also allow for more consistency in design and application of system of quality control frameworks within firms thereby allowing for third parties, such as corporate and governmental entities, investors, and peer firms to rely on and compare quality across firms.

Comment #2: Suite of quality management standards

ISQM 1 focuses on the firm-level system of quality control framework and, as a result, the PCAOB has proposed certain incremental considerations, some of which operate at the engagement-level. As noted by the IAASB, ISQM 1 is part of the IAASB’s suite of proposed quality management standards that include certain engagement-level controls. More specifically, ISQM 2, Engagement Quality Reviews (ISQM 2), provides an enhanced engagement quality review standard, and Revised ISA 220, Quality Management for an Audit of Financial Statements (ISA 220), provides for enhanced quality management at the engagement-level.

Rather than building from ISQM 1 and adding incremental considerations, we recommend the PCAOB consider incorporating the concepts in Proposed ISQM 2 and Proposed ISA 220 in its proposed revision to its current quality control standards. Doing so would further require an evaluation of and revisions to other existing applicable PCAOB standards where certain of these concepts are currently addressed.

Also, each of these proposed ISQM standards include Application and Other Explanatory Materials that are necessary for sufficient understanding of those standards. We recommend the PCAOB consider whether any incorporation or references to such proposed international standards should be inclusive of the application materials. The inclusion of or reference to the Application and Other Explanatory Materials may reduce the incremental considerations needed in a future quality control standard and drive consistency between the standards.

Comment #3: Incremental requirements

We recommend the PCAOB does not add incremental requirements in the development of PCAOB standards. It would be better to allow the implementation of the ISQM suite of standards to be put in place for a number of audit cycles before making changes to the approaches laid out in that suite of standards.

In the event a specific matter requires an incremental requirement, such requirement should be based on demonstrated persuasive incremental benefit to audit quality compared to maintaining the base established in the ISQM suite.

We agree with the PCAOB that individual firms are currently subject to several standards and maintaining compliance with multiple standards and the existence of “unnecessary differences in quality control standards could even detract from audit quality by diverting firms’ efforts from focusing on matters of fundamental importance to effective quality control systems.” Further, the concept release indicates “anticipate[d] incremental or alternative requirements” for firms performing engagements under PCAOB standards.

We agree with the PCAOB regarding the differences in standards, existing and proposed, and potential additional requirements. While we agree specific requirements may be necessary to comply with certain PCAOB standards and rules, a comprehensive principles-based, risk-based
approach with minimal differences from ISQM 1 and the related IAASB proposed quality management standards should be comprehensive to respond to various specific items.

Further, minimizing differences among quality control standards will promote consistency and comparability among domestic and international firms, which will enhance reliability and competition. Interested stakeholders should be able to evaluate and measure quality among firms regardless of jurisdiction using a consistent, known, and observable framework and, by doing so, we expect that firms will increasingly compete on quality.

Comment # 4: Scalability

As a matter of audit quality, registered firms serve as auditors to public companies and the complexities of such engagements should be responded to with a consistent minimum. Consequently, we expect the base quality management at registered firms to be comparable regardless of the relative size of the firm providing public company audits.

Comment # 5: Performance Measures

While performance measures may be helpful in many situations, we would like more information on how performance measures related to the achievement of audit quality objectives would be determined. By their nature, there is much diversity in the conduct of an audit based on the risk profile of the audit, as well as industry and client sophistication. The development of a standard set of performance measures would be challenging to complete and the relevance of its impact on audit quality would also be challenging to connect directly to all engagements. The risk profile of each engagement will determine many factors of engagement execution, including the level of staff, overall time commitment, allocation of time between engagement team members, and work allocation between engagement team members.

We believe the PCAOB should consider the many ways firms accumulate data related to the achievement of the various quality objectives and determine if there are universal methods to use. In addition, the PCAOB should indicate how performance measures will be evaluated. For example, will compliance be based on risk and a related percentage threshold or some other measure?

Comment # 6: Independent Directors

We do not believe a requirement for independent directors is necessary in the system of Quality Control.

Proposed IAASB ISQM 1 and the concept release include several items related to competencies, promotion to leadership roles, and overall experience. These competencies are developed through years of experience and exposure to and involvement in audits and other firm activities. Boards comprise individuals with extensive knowledge of the firm and the profession and, as a result of such knowledge, have been elected by their peers. We do not believe an independent director would have the same necessary qualifications or commitment to achieving high audit quality in a cost-effective manner.
Further, we do not believe that there is observable evidence that the use of independent directors is effective in improving audit quality within accounting firms as we believe that firms that have voluntarily adopted the use of independent directors have not utilized them in an oversight capacity as proposed by the PCAOB.

In addition, there may be unintended consequences of such requirements on the extent to which non-U.S. territories have adequate numbers of registered firms to meet the market requirements for PCAOB audits.

As many of these firms have a small number of audits of issuers, broker dealers, or components of such entities, a requirement to appoint independent directors may result in some of these firms surrendering their registration. This may increase the territories where issuers are either unable to or have extremely limited choices in the selection of an auditor.

Comment # 7: Implementation

The implementation of new standards can be a significant undertaking for firms. We believe the Board should consider the resources and time to design, document, implement, test, evaluate, and remediate a system of quality control in relation to ISQM 1 implementation and separately for any additional incremental requirements. This implementation process will be different for all firms and require all firms to increase and/or redirect resources to enable completion of newly required tasks.

In addition to the commitment from firm leadership needed to implement a new quality control standard as proposed by the Board, the execution of an enhanced quality control system will require involvement from many other individuals throughout the firm. Depending on the size of the firm, this will include individuals with responsibility for independence, human resources, learning and development, accounting guidance, auditing guidance, risk management, and others. Also, firms may have local office leadership, and regional or market leadership, which will need to be involved. This additional commitment also extends to Directors, Senior Managers, and Managers who lead audit engagements and the other professionals who perform audit engagements.

We expect it to take approximately 3 years to fully implement changes, including monitoring, from the time the PCAOB standard is finalized. The earliest this could be completed is December 31, 2023, assuming finalization of all related standards in 2020.

Comment # 8: Reasonable Assurance

We support the approach included in ISQM 1, whereby the system of quality control should be based on reasonable assurance and proactively managed to identify, evaluate, and remediate findings and deficiencies resulting in an ever evolving and improving system of quality control. Further, reasonable assurance should be applied and determined in the context of a systemic evaluation of the nature and extent of findings within a particular area rather than on the occurrence of a finding.
Questions and Answers:

We have included responses to the questions posed in the concept release in the attached appendix.

Conclusion:

We believe a system of quality control is an integral part of an audit practice and will continue to drive increases in audit quality. We fully support the PCAOB’s efforts to improve audit quality through a revision of its quality control standards.

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We appreciate your consideration of our comments and recommendations and would be pleased to discuss them with you at your convenience. Please direct any questions to Christopher Tower, National Assurance Managing Partner - Audit Quality and Professional Practice at 714-668-7320 (ctower@bdo.com) or Blake Wilson, Chief Compliance and Ethics Officer and National Partner - Audit Quality Assessment and Remediation at 214-259-1497 (bwilson@bdo.com).

Very truly yours,

BDO USA, LLP
Responses to Posed Questions:

I. Introduction:

Q. 1. 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?

As we noted in our general observations, we support the PCAOB in revising its quality control standards to address developments in audit practices and the profession.

Q. 2. Is it appropriate to use ISQM 1 as the basis for a future PCAOB QC standard? Are there alternative approaches we should consider?

We believe ISQM 1 is an appropriate basis for a future PCAOB quality control standard in order to minimize differences and enhance consistency and comparability of firms.

Q. 3. Are the reasons provided for differences between ISQM 1 and a future PCAOB QC standard appropriate? Are there other potential reasons for differences that we should consider?

We recognize there may be reasons for differences between proposed ISQM 1 and a future PCAOB standard based on unique U.S. market requirements. However, we recommend the PCAOB consider the nature of the differences and whether they are considered within the principles-based, risk-based nature of ISQM 1 and minimize unnecessary differences. We believe a principles-based, risk-based standard would provide for proper implementation and execution.

Q. 4. Are there other developments affecting audit practices we should consider addressing in a future PCAOB QC standard?

As the overall audit environment changes, additional technological and data analysis audit techniques will be included in procedures performed and utilized by audit firms throughout the conduct of an audit. Further, firms are experimenting with improved approaches to engagement staffing models. Any proposed quality control standard will need to be sufficiently flexible to account for future technology changes, audit automation advances, and new engagement staffing models.
II Background and Consideration for Potential Revisions to QC Standards

Q. 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 system?

As firms monitor the activities of the various standard setting bodies, such as IAASB, PCAOB, and AICPA, firms are constantly reviewing existing procedures and making improvements or changes where necessary to stay in compliance with changes in standards. Currently, as firms anticipate adoption of ISQM 1 and the related suite of standards, we understand that firms vary in their levels of progress, including some that may be in early stages of risk assessment while others may have already completed a few testing cycles. We believe we share an industry view that effective implementation of the proposed ISQM standards and a revised PCAOB quality control standard will require considerable effort and take a few years to be fully effective. Further, we note that certain system of quality control enhancements in certain areas may take multiple audit cycles to result in observable improvement in audit quality.

Q 6. Please provide references to any academic studies or data we should consider, including academic studies or data that might address costs and benefits relevant to an economic analysis of potential revisions to PCAOB QC standards.

We will not be providing comment on this question.

III Potential Standard-setting Approach Based on Proposed ISQM 1:

Q. 7. Would the approach to quality control standards described in this concept release be preferable to the current PCAOB quality control standards?

We believe the approach in the PCAOB’s concept release, which would require a more proactive and interactive management approach, to be more in line with the current environment. Theoretically, active monitoring and remediation should result in fewer findings and increased quality.

In addition, as proposed ISQM 1 and its related quality management standards include a principles-based, risk-based approach, we would expect minimal incremental requirements.

Q. 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 that the overall objective of the firm as stated in the proposed ISQM 1 is an appropriate comprehensive statement and that no additional objectives are necessary:

“The objective of the firm is to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements performed by the firm, that provides the firm with reasonable assurance that:
Appendix to BDO’s Response to PCAOB Concept Release 2019-003

(a) The firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and

(b) Engagement reports issued by the firm or engagement partners are appropriate in the circumstances.”

Q. 9. Would the potential revisions to PCAOB QC standards described in this concept release improve QC systems and audit quality?

We believe the newly proposed components, such as governance and leadership, information and communication, and risk assessment, as included in ISQM 1, should have a positive impact on audit quality due to a more acute focus on resources and accountability for quality. Further, specific recognition of technological and intellectual resources and of third-party service providers will bring more modern considerations to the standard and consistent controls around the use of audit tools and technology.

Q. 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?

We believe that many of the potential revisions described in ISQM 1 will lead to a stronger system of quality control and an overall increase in audit quality. As noted in various other question responses, we believe that certain of the revisions will have more of a direct impact on audit quality than others, and the cost and resulting minimal or indirect impact of other proposed revisions may outweigh their practicality. As audit deficiencies are unique in nature, it is difficult to predict the impact the system of quality control will have on audit deficiencies. While the goal is to have zero audit deficiencies, a measure of reasonable assurance should continue to be applied.

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

We believe the same risk-based, principles-based system of quality management as considered in proposed ISQM 1, which is scalable, is appropriate for use by firms that audit broker dealers.
IV. Specific Aspects of a QC System and Potential Changes to PCAOB Standards

Q. 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?

It is difficult to estimate the costs and benefits of implementing and maintaining an integrated, proactive quality control system as described in the concept release. Additional dedicated resources, including dedicated leadership time, will be needed to identify, evaluate, and remediate findings and deficiencies; monitor and evaluate corrective actions; and aggregate information and evaluate whether such information is determinative of an effective system of quality control under a reasonable assurance framework. Such impacted resources will not be limited to the assurance practice but may also include those in other departments such as Human Resources and Finance. Further, depending on a firm’s organizational structure, there could be different processes in different regions that may need to be aligned to enable comparability and consistency, or different testing approaches designed to accomplish the same objectives. Given the nature and scope of the PCAOB Concept Release, it is reasonable to conclude that the costs would be substantial and have an adverse economic impact to a firm.

A. Firm Governance and Leadership:

Q. 13. Is the approach to firm governance and leadership 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?

We believe that the inclusion of governance and leadership, as included in ISQM 1, is appropriate. A firm’s culture, as exemplified by its leadership, is a strong driver of audit quality. Similar to the COSO 2013 Internal Control - Integrated Framework, the “tone at the top…the importance of internal control including expected standards of conduct”, a firm’s leadership is responsible for the tone of the firm and its overall direction, which includes audit quality.

As a matter of regulatory principle, it is our view that the operational arrangements, decisions around business practices, the composition of senior leadership, and the allocation of resources are best determined by the regulated entity. Impacting the ability of firms to appoint leaders based on their needs and strategy, how the firm establishes its governance structures, and the operational allocation of resources may negatively impact the competitive nature of these firms. Such approaches may also inhibit advances in innovation and development of new approaches to audit execution, which may ultimately detract from advances in audit quality.

As a consequence, we believe that the principles laid out in the ISQM suite adequately address the objectives of appointing senior leaders with appropriate experience and focus on quality, of establishing firm governance and leadership that is suitable to the firm’s context, and in facilitating the allocation of resources to achieve the objectives of audit quality.
Q. 14. Would more clarity in the assignment of firm supervisory responsibilities enhance supervision and positively affect QC systems and audit quality?

We believe a proposed standard should clearly define the objectives and allow for each firm to design its system to meet the objectives. Given the various size firms and different leadership structures, this will be different in each firm and needs to be able to change as firms change and the environment evolves.

Paragraphs 23 through 25 of proposed ISQM 1 outline the responsibilities, experience, and knowledge of the individuals assigned ultimate and operational responsibilities for the firm's system of quality control. Further, paragraphs A36 through A39 within the application guidance provide additional clarity as to these supervisory responsibilities, which appears sufficiently flexible given the variety of sizes and structures that exist among firms. Paragraph A38 also provides for the ability to further assign roles, procedures, and tasks or actions to other individuals under the authority and supervision of the individual with operational responsibility, and paragraph A39 indicates that based upon facts and circumstances, firms could set additional eligibility criteria beyond what is in ISQM 1 for the individual assigned operational responsibility. As a result, we do not believe that additional clarification is necessary based on the ISQM 1 application guidance.

Q. 15. Should a future PCAOB QC standard address quality considerations in the appointment of a firm’s senior leadership? If so, how?

Proposed ISQM 1 requires, among other considerations, that individuals assigned ultimate and operational responsibility for the firm’s system of quality management have a sufficient understanding of the ISQM requirements and be subject to annual performance evaluations. Such evaluations should consider the outcome of the evaluation of the system of quality management. Further, as noted in the ISQM 1 application guidance, how firms assign roles and responsibilities and authority varies by firm and may be impacted by certain jurisdictional laws and regulations. Therefore, we believe that each firm’s process in accordance with ISQM 1 for the appointment of firm leadership would be sufficient.

Please also see our response to question # 13 regarding firm leadership.
Q. 16. Allocation of financial resources is one aspect of firm governance and leadership under Proposed ISQM 1. Should this be given greater emphasis in a future PCAOB QC standard than it is given in Proposed ISQM 1? For example, should a future PCAOB QC standard emphasize the importance of counterbalancing commercial interests that may lead to underinvestment in the audit and assurance practice, particularly in firms that also provide non-audit services?

Additional emphasis or specificity beyond what is included in ISQM 1 seemingly would be difficult to design, implement, and monitor in a consistent manner given the complexities associated with the design and operation of each firm’s structure and organization. ISQM 1 paragraph 23 indicates that firms are required to plan, obtain, allocate and assign resources in a manner that support the firms’ commitment to quality. Sufficient fulfillment of this requirement is contingent upon qualified, knowledgeable individuals within a firm evaluating numerous assumptions that change year to year. Additionally, application guidance within ISQM 1 notes that individuals assigned ultimate and operational responsibility for the system of quality management are in most instances able to influence the nature and extent of resources the firm allocates or assigns to support a commitment to audit quality, and these same individuals are subject to annual performance evaluations that include consideration of the system of quality management. The performance evaluations provide a sufficient counterbalance to possible underinvestment in the audit and assurance practice.

Please also see our response to question # 13 regarding firm leadership.

Q. 17. Should a future PCAOB QC standard incorporate mechanisms for independent oversight over firms’ QC systems (e.g., boards with independent directors or equivalent)? If so, what criteria should be used to determine whether and which firms should have such independent oversight (e.g., firm size or structure)? What requirements should we consider regarding the qualifications and duties of those providing independent oversight?

Proposed IAASB ISQM 1 and the concept release include several items related to competencies, promotion to leadership roles, and overall experience. We do not believe an independent director would have the same qualifications or commitment to achieving high audit quality in a cost-effective manner. Therefore, we believe the use of independent oversight should remain as an optional response to a risk assessment determination or an optional remedial action to a set of findings.

Further, we do not believe that there is observable evidence that the use of independent directors is effective in improving audit quality within accounting firms, as we believe that firms that have voluntarily adopted the use of independent directors have not utilized them in an oversight capacity as proposed by the PCAOB.

Please also see overall comment # 6 regarding our position on independent directors.
B. The Firm’s Risk Assessment Process:

Q. 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?

We believe the approach to risk assessment, as included in ISQM 1, appears appropriate.

Q. 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 principles-based requirements are sufficient. A principles-based approach provides for scalability within a firm and within the risk assessment. A firm will be able to determine the potential impact a risk may have on audit quality and the system of quality control and then document its conclusion. In addition, based on the risk, a firm will design an appropriate response and related testing as applicable.

Q. 20. Should a future PCAOB QC standard specify certain quality risks that must be assessed and responded to by all firms? If so, what should those risks be?

Risks evolve and change over time. Defining certain quality risks within the standard may increase the likelihood that the standard will become obsolete rather than dynamic over time. Instead, the PCAOB has other communication methods available, such as through speeches or 4010 reports, that provide the PCAOB with a real-time forum for communicating relevant risks that should be expected to be addressed. In addition, as time progresses, we recommend the PCAOB consider methods to remove previously prescribed or required risks due to changes in circumstances or the business environment. This would help to limit the growth of requirements and maintain the relevance of any risks or processes identified.

Q. 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 do not believe that firms should be required to establish quantifiable performance measures for the achievement of quality objectives. Currently, there is no commonly accepted definition of “audit quality” and many factors are assessed when determining whether audit quality has been achieved at both the firm level and specific engagement level. No one specific measure is determinative or predictive, and the assessment must be qualitatively considered in context of the specific facts and circumstances. Accordingly, setting quantifiable measures would require assessing the aggregate impact of those measures achieved and those measures not achieved. This would be a highly complex and subjective process.

Having said this, performance measures may be helpful indicators, providing meaningful assessment tools for firms to use to guide where focus and remediation is necessary. Further, if performance measures were required, we would like more information on how performance measures related to the achievement of quality objectives would be determined. In doing so, we
recommend the PCAOB consider the various ways firms accumulate data and information related to the achievement of the objective and determine if there are universal methods to use. In addition, we recommend the PCAOB indicate how performance measures will be evaluated. For example, will compliance be based on minimum acceptable thresholds, will relative risk and significance of an indicator impact its importance in the assessment process, and will each indicator be assessed individually, or will the indicators be assessed in the aggregate?

C. Relevant Ethical Requirements:

Q. 22. Is the approach to relevant ethical requirements 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?

We support the use of ISQM 1 as a basis for relevant ethical requirements.

Q. 23. Should a future PCAOB QC standard extend detailed requirements for independence quality controls (formerly SECPS member requirements) to all firms? How would this affect the costs and benefits of a QC system?

We agree that independence quality controls should be consistently applied to all firms, inclusive of many of the former SECPS member requirements. However, in doing so, we recommend that the PCAOB evaluate and revise certain of the Appendix L requirements.

More specifically, we agree with reporting any “material” independence violation, and we agree with the proposal to replace a “senior-level” partner with a “qualified individual with appropriate knowledge, skill, ability, capacity, and authority to assume responsibility for independence.” We also note that communications with audit committees is generally an engagement-level activity. Obtaining information relevant to PCAOB Rules 3524, 3525, and 3526 is often a mix of firm and engagement level processes; therefore, we believe that more clarity is needed to understand what the PCAOB’s intent is with such a firm-level communication requirement.

D. Acceptance and Continuance of Clients and Engagements:

Q. 24. Is the approach to acceptance and continuance of clients and engagements 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?

The approach appears appropriate as stated in proposed ISQM 1.
E. Engagement Performance:

Q. 25. Is the approach to engagement performance 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?

The approach appears appropriate as stated in proposed ISQM 1.

Q. 26. Should a future PCAOB QC standard expressly address firm responsibilities and actions to support and monitor the appropriate application of professional skepticism and significant judgments made by engagement teams? If so, how?

We support the existing emphasis placed upon professional skepticism as noted in proposed ISQM 1 and in various instances in proposed revised ISA 220. Further, we believe that PCAOB AS 1015, paragraphs .07 through .09 also provide sufficient emphasis. The exercise of professional skepticism is an engagement-level activity that is the responsibility of the engagement partner and subject to the engagement quality control review, and we believe that a future firm-level monitoring activity may not be in the spirit of principles-based standards and scalable across all firms.

Q. 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 agree that a future quality control standard should address the use of other audit participants, including the use of specialists and service centers to support audit engagements; however, it may be better to include such a requirement within the Resources component.

Q. 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 believe there is value to the existing Appendix K review. The requirement was implemented prior to the PCAOB requiring foreign firms serving U.S. issuers to register. While such firms should have sufficient understanding and experience with PCAOB Standards and SEC filing requirements, the consistent and contemporaneous involvement that U.S. firm personnel have with such requirements generally adds value to filings associated with foreign registered firms.
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Q. 29. Should a future PCAOB QC standard require firms to adopt engagement monitoring activities (e.g., performance measures, engagement tracking tools, or reviews of in-process engagements) that would prompt them to proactively prevent or detect engagement deficiencies? What are examples of less formal, but effective, engagement monitoring activities that could be adopted by smaller firms?

We believe the adoption of performance measures, engagement tracking tools, or reviews of in-process engagements should remain as optional responses to specific risks. Further, performance measures, which are typically quantifiable measurements that the profession has referred to as Audit Quality Indicators, are not widely agreed to or accepted without specific qualitative context that would be associated with specific risk assessments.

We have provided our views on Audit Quality Indicators to the PCAOB in our response to Concept Release No. 2015-005. We welcome further discussion regarding the development, use, and comparability of Audit Quality Indicators.

Q. 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 the existing requirements are sufficient to address auditor’s responsibilities under Section 10A of the Exchange Act or going concern considerations. We do not believe that a future PCAOB QC standard should have additional provisions to items a, b, and c above. Specifically, ISQM 1 adequately addresses considerations regarding compliance with laws and regulations, accounting standards, and auditing standards.

Additionally, the items noted above are addressed in other PCAOB standards:
   • AS 2401 - Consideration of Fraud in a Financial Statement Audit
   • AS 2405 - Illegal Acts by Clients
   • AS 2415 - Consideration of an Entity’s Ability to Continue as a Going Concern.

F. Resources:

Q. 31. Is the approach to resources 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?

The approach appears appropriate as stated in proposed ISQM 1.
Q. 32. Should a future PCAOB QC standard continue to expressly address technical training on professional standards and SEC requirements? Are there other subjects for which training should be expressly required? Which firm personnel should be covered by the training requirements? Should the standards set minimum requirements for the extent of training? If so, what should those requirements be based on?

We believe proper training and education of professionals leads to high-quality audits. Professionals should receive training appropriate for their level as they progress and advance in their careers. Therefore, a future PCAOB quality control standard should address technical training on professional standards and SEC requirements. We believe that specific issuer related training below the senior level would not be required, and there should be different levels of training for seniors, managers, and partners to be responsive to their respective roles and responsibilities.

SECP Section 1000.08(d) requires that “all professionals in the firm residing the United States, including CPAs and non-CPAs, participate in at least 20 hours of qualifying continuing professional education every year and at least 120 hours every three years.” While such an educational requirement is beneficial to individuals, it is not necessarily relevant to all firm professionals, many of whom provide professional services in other business lines that are not relevant to issuer audits. We recommend the PCAOB revise and incorporate Sections 1000.08(d) and 8000 as relevant to the current environment within a new proposed quality control standard.

Q. 33. Should a future PCAOB QC standard continue to expressly address required competencies of engagement partners? Are the competencies discussed in this concept release appropriate? Are there other competencies that should be added?

We believe that the required competencies of engagement partners as included within PCAOB QC 40 – The Personnel Element of a Firm’s System of Quality Control Competencies Require by a Practitioner-in-Charge of an Attest Engagement, would be appropriate as an incremental requirement to ISQM 1; however, we are supportive of the principles-based approach outlined in proposed ISQM 1.

Q. 34. Should the competencies of individuals in engagement or QC roles, in addition to the engagement partner and engagement quality reviewer, be addressed in a future PCAOB QC standard?

We believe the approach in ISQM 1, which indicates “human resources with the appropriate competencies and capabilities, including sufficient time, to perform” such activities, to be appropriate. Given the varying nature of firms, more specific competency requirements for roles other than the engagement partner and engagement quality reviewer may result in a lack of scalability.
Q. 35. Should a future PCAOB QC standard expressly address the use of emerging technology in QC systems or engagements? Should a future PCAOB QC standard expressly require firms to design and implement controls to prevent unauthorized access to technology and data? Are there any other requirements we should consider related to the use of technology on engagements?

As the auditing profession changes and evolves, professional standards will need to be adaptive to different and enhanced methods of auditing. Our clients are increasingly using more advanced technology and are demanding we do the same in the execution of our audits. We embrace technology for better auditing and would expect that engagement partners have a sufficient understanding of data analysis used within an audit, but not necessarily the computer science associated with the analysis or technology employed. Instead, we would expect to have sufficient firm-level controls around approved and tested applications and models.

We believe that any future quality control standard should address the risk of unauthorized access, with a requirement of firms to respond to significant risks identified through the design and implementation of relevant controls. Such future quality control standard should acknowledge the complexity of the technology landscape and that no design provides absolute assurance that unauthorized access can be prevented.

As technology advances, so do ways to abuse the technology. We acknowledge that cyber security is an ongoing issue that affects all companies, as prevention of all forms of data breaches is an elusive goal, and state and federal governments around the globe are holding corporate entities, including firms, accountable for data and privacy breaches.

Q. 36. Ensuring that firm personnel in QC and engagement roles have sufficient time to properly carry out their responsibilities is one aspect of firm resources under Proposed ISQM 1. Should a future PCAOB QC standard place greater emphasis on this requirement than Proposed ISQM 1 does? If so, how?

We agree with the proposal in ISQM 1 regarding sufficient time for engagement partners and engagement quality control reviewers and recognize it is part of a well-executed high-quality audit. As each engagement is unique, the amount of time required by engagement partners and engagement quality control reviewers, as well as the timing of the work, will vary from audit to audit; however, we do not believe that additional emphasis is necessary.

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

We believe performance management, as addressed in the Resources component of ISQM 1, sufficiently incorporates quality considerations such that no additional emphasis is necessary.
G. Information and Communication:

Q. 38. Is the approach to information and communication 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?

The approach appears appropriate as stated in proposed ISQM 1.

Q. 39. Should a future PCAOB QC standard require public disclosure by firms about their QC systems? If so, what should be the nature and timing of such disclosures (e.g., information about the firm’s governance structure)? (see also Question 46)

We do not believe that a requirement to publicly disclose information about a firm’s system of quality control is consistent with PCAOB Rule 4009 or Sections 104(g)(2) or 105(b)(5)(A) of the Sarbanes-Oxley Act. Any such requirement considered by the PCAOB should not infringe on the firm’s confidentiality protections afforded by Sections 104 and 105 of the Sarbanes-Oxley Act. Further, we are supportive of, and participate in the practice of, voluntary publishing of our audit quality report and do not believe it is necessary to publish a transparency report or equivalent document.

H. The Monitoring and Remediation Process

Q. 40. Is the approach to the monitoring and remediation 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?

The approach appears appropriate as stated in proposed ISQM 1.

Q. 41. Would the requirements related to monitoring and remediation discussed in this concept release prompt firms to develop an appropriate mix of ongoing and periodic monitoring activities? Would the requirements create an appropriate feedback loop to prevent future engagement deficiencies?

We believe the approach noted within ISQM 1 is appropriate and allows for a scalable application of the proposed standard. While we agree that ongoing monitoring will provide more timely information, the nature of certain audits may not lend themselves to “an appropriate mix of ongoing and periodic procedures.” Instead, paragraph A156 within the application guidance of ISQM 1 states that “[t]he firm’s monitoring activities may comprise ongoing monitoring activities, periodic monitoring activities or a combination of both. In most cases, ongoing monitoring activities identify findings in the system of quality management in a timelier manner.” Under a principles-based, risk-based approach, firms should have flexibility in designing and performing monitoring procedures.
Q. 42. Should a future PCAOB QC standard provide additional direction regarding determining appropriate monitoring procedures, appropriate root cause analysis, and remediation of QC and engagement deficiencies? If so, what type of direction is needed?

We believe additional direction would be helpful in determining appropriate monitoring procedures. We recommend the PCAOB consider the ISQM 1 application guidance as a basis for monitoring and root cause procedures. More specifically, many firms may not have established a formal cause analysis program and may need guidance in developing a sufficient program. The guidance provided in paragraphs A179 through A182 within the application guidance of proposed ISQM 1 provides some relevant guidance that may need further emphasis. However, in providing any such guidance, we believe that it should be principles-based without endorsement of any specific cause analysis model. Further, if not provided within ISQM 1, we recommend the PCAOB, with evaluative feedback from the profession, establish a framework for evaluating the severity of findings and the impact that those findings have on establishing reasonable assurance that the system of quality control is effective.

Q. 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?

We believe internal inspections are a key element of a firm’s monitoring procedures and should be included in a system of quality control. The data developed through internal inspections enables a firm to identify audit quality events, both positive and negative, that drive future enhancements and changes to the audit process.

Q. 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?

If a requirement to perform inspections of completed engagements is retained, we believe each firm will design selection criteria that appropriately address each firm’s risk assessment and audit profile. We do not believe minimums or set requirements would be necessary and could result in a compliance audit rather than a risk-based process designed to identify audit quality events, positive and negative, across the firm and its partners.
Q. 45. Should firms be required to perform an annual evaluation of their QC system’s effectiveness? If so, should the required evaluation be as of a specified date or for a specified period? How should the date or period be determined?

We believe firms should evaluate the effectiveness of their quality control systems on an annual basis, with the evaluation being as of a specified date. Determination of the as-of date should be flexible, as it may be appropriate for some firms to correspond the date with the firm’s fiscal year while other firms may find it beneficial to set the date at a natural break in the monitoring cycle, which may not correspond with the firm’s fiscal year end.

Q. 46. Should firms be required to report to the Board on their annual evaluations of QC system effectiveness? If so, what should be included in the report? Should firms be required to disclose any performance measures that were important to their conclusion about their QC system’s effectiveness? Should firm reports be publicly available (see also Question 39)?

We believe the Board should consider providing additional information for a firm’s annual evaluation, specifically, guidance on evaluating the overall effectiveness of the system of quality control in accordance with a reasonable assurance model.

We do not believe a formal report to the PCAOB or to the public would be necessary. Instead, annual assessments will be subject to PCAOB inspections and available to inspection teams upon their request.

Q. 47. Should we require the firm’s top leadership to certify as to their QC system’s effectiveness, either as part of or in addition to the firm’s report on their QC system’s effectiveness?

We are supportive of the system of quality management evaluation performed by the individual assigned ultimate responsibility and accountability included in proposed ISQM 1 and do not believe that additional enhancements would add value.

I. Documentation:

Q. 48. Is the approach to documentation 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?

The approach appears appropriate as stated in proposed ISQM 1.

Q. 49. Are the potential sufficiency and retention period requirements described in this concept release appropriate for a QC system? Why or why not? If not, what alternatives should we consider?

We noted the concept release indicates the PCAOB is considering a documentation standard similar to AS 1215. We agree with the requirement to maintain documentation of the quality control system and the basis for the firm’s assessment.
We recommend the PCAOB provide additional information related to documentation requirements, as certain aspects of AS 1215 may be difficult to apply to a system of quality control.

By analogy, we note that when performing an audit of internal control over financial reporting, tested controls are part of a recorded transaction. In accordance with ISQM 1, a firm is required to identify quality objectives and related responses. In some instances, these responses may be a firm policy, firm designed form, or practice aid. As noted in ISQM 1, A212 “Documentation may take the form of formal written manuals, checklists and forms, may be informally documented (e.g., e-mail communication or postings on websites), or may be held in IT applications or other digital forms (e.g., in databases).” These types of responses may not be part of a population of transactions that would be subject to testing. Additional guidance will be necessary for the documentation required for these types of responses. In addition, ISQM 1, A214 indicates “In a smaller firm, it may not be necessary to have documentation supporting matters communicated because informal communication methods may be effective. Nevertheless, the firm may determine it appropriate to document such communications in order to provide evidence that they occurred.”

We believe additional information for documentation requirements should be provided in a revised standard of quality control.

As noted in our response to question 46, the Board should consider providing a method for evaluating effectiveness.

Q. 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 believe that proposed ISQM 1 includes sufficient documentation of networks and third-party methodologies and tools due to required documentation to support a consistent understanding of the quality control system and to support the consistent implementation and operation of responses. As a result, we do not believe that more specific documentation requirements are necessary beyond requirements included in proposed ISQM 1.

J. Roles and Responsibilities of Individuals

Q. 51. Should a future PCAOB QC standard specify roles and responsibilities of firm personnel in relation to the firm’s QC system?

We are supportive of specification of roles for individuals having ultimate and operational responsibility for the firm’s system of quality control and of the role for responsibility for independence quality control as outlined in proposed ISQM 1. We do not believe that incremental requirements associated with these roles or other roles is necessary.
Q. 52. Are the roles and responsibilities described in this concept release appropriate? Are there other roles that should be added (e.g., chief ethics officer, chief technology officer)? Are there further responsibilities that should be added?

The roles related to ultimate and operational responsibility and independence quality control are appropriate. The Concept Release includes consideration of specific responsibilities of all firm personnel; however, these requirements are included in existing PCAOB standards and may be duplicative unless the existing standards will be superseded. For instance, maintaining professional competence, integrity, objectivity, and due professional care are required within:

- AS 1001: Responsibilities and Functions of the Independent Auditor
- AS 1005: Independence
- AS 1010: Training and Proficiency of the Independent Auditor
- AS 1015: Due Professional Care in the Performance of Work

V. Related Potential Changes to Other PCAOB Standards

Q. 53. Are the potential amendments to AS 2901 appropriate? Are there other approaches we should consider to prompt firms to appropriately respond when there are indications calling into question the sufficiency of audit procedures performed and/or audit evidence obtained?

We believe the current standards in AS 2901 are appropriate. Specifically, paragraph .04 provides for a risk-based approach that enables the auditor to “assess the importance of the omitted procedures to his present ability to support his previously issued opinion...the results of other procedures that were applied may tend to compensate for the one omitted or make its omission less important.”

Q. 54. Does AS 1110 provide helpful direction to auditors, or should it be rescinded? Please provide explanation for your answer.

Similar to the suite of proposed ISQM standards, we believe that AS 1110 provides appropriate linkage between firm-level and engagement-level activities. While we are supportive of retaining AS 1110, we would also be supportive of the PCAOB considering enhancements to AS 1110 that bring it into congruence with proposed revised ISA 220.

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

The list of Primary PCAOB Standards Affected included in the concept release new standard appears complete.
VI. Scalability

Q. 56. We intend that a future PCAOB QC standard developed using this approach would be applicable to all firms and scalable based on their size and complexity and the nature of their engagements. What factors should we consider when developing a future PCAOB QC standard to ensure that its requirements are appropriately scalable?

As discussed throughout our response, we agree it is important that a future PCAOB QC standard that is applicable to all firms be principles-based, risk-based, and scalable to a firm’s risks, complexity, and the nature of its engagements. This scalability will need to consider the complexities of auditing in accordance with PCAOB standards. We encourage the Board to minimize requirements that are prescriptive in nature.

Q. 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 that many smaller firms likely will incur significant costs associated with implementation of proposed ISQM 1, particularly those that may only be subject to ISQM 1 as a result of conducting audits under PCAOB standards. For instance, many smaller firms may not have formalized monitoring and remediation processes. Complying with ISQM 1 will likely cause these firms to require additional experienced quality control resources, and any prescriptive, incremental requirements within a revised PCAOB quality control standard will only exacerbate the situation.

Q. 58. Should we have additional, more specific requirements regarding certain components or areas (e.g., governance and leadership) for larger, more complex firms or based on the nature of engagements performed by the firm (e.g., broker and dealer engagements or engagements for issuers in specialized industries)? If so, what should those be?

We do not believe additional, more specific requirements would be necessary. As discussed in this letter, we believe example processes, responses, and controls would be helpful in implementing a new quality control standard. These examples would help a firm design and implement a quality control system that is appropriate based on firm-specific risks. This would enable scalability across all firms.

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