

September 29, 2015

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

Via email: [comments@pcaobus.org](mailto:comments@pcaobus.org)

**CONCEPT RELEASE ON AUDIT QUALITY INDICATORS (AQIs)  
PCAOB Release No. 2015-005**

Dear Sir/Madam,

The International Federation of Accountants® (IFAC®) values the opportunity to comment on the Public Company Accounting Oversight Board (PCAOB)'s abovementioned concept release (CR). IFAC welcomes the PCAOB's efforts to enhance understanding and dialogue on audit quality, and commends the PCAOB on its approach of consulting widely on these important matters.

Through its current membership of more than 175 professional accountancy organizations in 130 countries and jurisdictions, IFAC represents approximately 2.8 million accountants in public practice, industry and commerce, government, and education. As such, it aims to provide the perspective of the global accountancy profession.

IFAC supports the innovative approach taken in the CR, toward new ways of understanding and gaining wider perspectives on audit quality. We welcome the emphasis in the CR on the need to consider quantitative indicators in their qualitative context, and the recognition of inherent limitations of indicators. However, as the PCAOB progresses to phasing-in the concept, we would urge that it further clarifies the objectives of the initiative and addresses the associated risks.

It is encouraging to observe the congruence—at a high level—of the PCAOB's AQI model with many aspects of the International Auditing and Assurance Standards Board®'s *Framework for Audit Quality* (the Framework), issued in 2014, noting that the CR is more focused specifically on the quality of audits, rather than audit quality more generally within a jurisdiction. For example, the CR deals with a model of audit professionals, audit processes, and audit results; this corresponds well with the Framework's model, dealing with input factors, process factors, and output factors (in addition to key interactions and contextual factors).



### *Impact and Use*

The manner in which quality and performance are measured acts as a powerful incentive, which can have a profound impact on the behavior of those concerned. In forming and implementing the concept, it is critical to clearly identify and address both intended and unintended effects.

As is the case in any regulatory or quasi-regulatory measure, clarity and appropriateness of objectives is a central factor in determining success or failure. There is scope for greater clarity between multiple objectives, which are emphasized to differing extents throughout the CR:

- Informing and prompting discussion or questions;
- Signaling audit quality; and
- Promoting competition on audit quality.

Clarity around objectives is particularly important to maximize the value of the concept; for instance, in enhancing understanding of and dialogue toward improving audit quality, while managing the risk of a compliance or checklist-driven approach.

The CR clearly details that there are limitations inherent in indicators, qualitative context is important, and they “are not algorithms, benchmarks, or safe harbors against enforcement or other claims, and they do not lead directly to formulas.” However, there is scope to more comprehensively address the risk that formally recognizing such indicators and advocating their use by audit committees, investors, and regulators would lead to them being used in a formulaic manner without appropriate context.

An important aspect in addressing this risk is to determine clearly who is considered the appropriate audience for AQIs, in view of the contextual information they would have access to and are likely to have command of. For example, audit committee members are likely to have access to fuller context and background, as well as the ability to inquire as needed.

### *Audit Quality and Competition*

IFAC urges caution with respect to the suggestion of seeking to create “incentives for competition in quality” among audit firms. Promoting competition toward innovation that aids quality, and differentiation based on specialization, are considered highly appropriate. However, promoting competition around an implied variability in audit quality may not always be considered appropriate and in the public interest—audit quality should rather be a nonnegotiable, fundamental goal for all audits. Experimenting with incentives for competition in audit quality also risks an adverse impact on quality, and may lead to competition on price.

### *Nature of the Indicators*

Some of the AQIs contemplated in the CR reflect detailed operational measures; for example, ‘staffing leverage,’ ‘partner workload,’ and ‘turnover of audit personnel.’ While these may be in some respects relevant, a resulting risk is that external focus on these measures, if not appropriately calibrated, may lead to unnecessary complexity and effort and be a distraction for auditors, regulators, and other participants in the wider financial reporting supply chain. As recognized in the paper, scalability of this approach also creates significant complexity. For instance, where small- and medium-sized practices (SMPs) cannot



provide information on all AQIs because of the nature and size of their business, there is a possibility this could lead to an unfair assumption that SMPs perform lower-quality audits.

Additionally, some of the AQIs appear to be more within the control of company management or others in the financial reporting supply chain than auditors—in particular, the “financial statement” measures. This highlights the nature of audit quality as an interdependent part of the wider financial reporting supply chain, and further illustrates why attempting to incentivize firms to compete on quality—and focusing on the AQIs—could be counterproductive.

*Implementation*

IFAC supports a “phase-in over time” approach to implementation, as outlined in the CR. As indicated in the CR, this approach is more likely to enable a feedback loop that could inform the optimization of the concept, ensure consistency of implementation, and allow for risks and issues to be identified and dealt with.

Please do not hesitate to contact us should you wish to discuss any of the matters raised in this letter.

Regards,

A handwritten signature in black ink, appearing to read "Faye Choudhury", written over a light blue horizontal line.

Faye Choudhury  
Chief Executive Officer