

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

Re: PCAOB Audit Quality Indicator; Response to 2015-005,

September 29, 2015

Dear Public Company Accounting Oversight Board:

Initially, we must begin by acknowledging the quality of the overall document which was prepared by the PCAOB. The document and approach are clear, concise and well-conceived.

Our response is intended to enhance and extend the work.

### **Response Overview**

It is our recommendation that in order for Audit Quality measures to be effectively implemented, they must be part of a framework based internal control program at each firm.

We believe that the most significant measures are performance related at the engagement level. The determination of the specific measures that should be monitored would be agreed to by the Audit Committee and the Audit Firm for each engagement.

Internal controls at each firm would monitor for compliance and remediate any circumstances where the firm was unable to achieve the agreed upon quality measures.

Firm level measures would be developed and monitored by the firm based on the firm specific requirements.

PCAOB and other regulators could determine a minimum set of aggregate reportable quality performance metrics which could be required to be reported.

### **Key Issue Discussion**

#### **Audit Quality, Internal Controls, and Audit Risk**

The relationship between Audit Quality, Internal Controls, and Audit Risk is strikingly similar to the objectives, controls and risks of Internal Controls over Financial Reporting (ICFR). The solution should be a program of defined objectives, internal controls, risk controls matrix, monitoring controls, and testing aimed towards the achievement of Quality Audits of Public Companies.

The solution should not be too prescriptive. Evaluation of Audit Quality should follow an established Framework (potentially "COSO") and have a set of quality objectives at both the entity level (firm) and engagement level. The firm should establish risk and quality indicators at the firm level related to entity controls designed to monitor quality of firm wide initiatives such as training and remediation efforts.

A key part of any control structure is the establishment and monitoring of objectives and controls related to the performance of key activities at a level of granularity which could detect and correct items which could be material risks toward the completion of the overall objective. In the audit world, this would be engagement level objectives, risk and controls designed to prevent degradations of audit quality which could lead to audit failures.

**We strongly recommend that an audit quality compliance program similar to Sarbanes-Oxley compliance programs be instituted, monitored, audited and reported on at each public accounting firm.**

**The program would be instituted, designed and placed into effect by each firm based on their unique risks, structures, client base, and working practices.**

### **Moving a Program Forward**

In order to move the program forward, a requirement that each firm design, implement and monitor an Audit Quality program within the above guidelines would offer the firms a chance to create programs which are best suited, most cost effective and most relevant to ensuring quality.

### **Prescriptive Requirements**

Although the prescriptive requirements should initially be kept to a relative minimum, the PCAOB could prescribe certain Quality measures which it believes would be required, strongly recommended, or suggested.

Additionally, certain definitional values should be standardized such as industry codes and other parameters used to aggregate data. The PCAOB could provide guidance and determinations to ensure better data quality and comparability.

### **Framework for Audit Quality**

#### **Unit of Measure Consideration**

Audit Quality measures at all levels of unit of measure are important.

Our response is built on a premise that the most important level is the audit engagement unit of measure for four reasons;

- 1) failure variations occur at the engagement level,
- 2) higher level unit measures can be built from properly aggregated engagement level statistics.
- 3) engagement level failures indicate ineffectiveness of firm level controls, and
- 4) engagement level process quality performance indicators can serve as monitored preventative operational controls beneficial to timely detection of quality issues requiring performance adjustment remediation.

***We expect the most common and vociferous response to assert that aggregation at the engagement level is impractical.***

***Failure variations*** - Audit quality varies significantly within the same firm. Based on the results of the PCAOB's ongoing inspections, there is ample evidence of this wide variation of audit quality at each of the larger firms. Most firms perform both acceptable quality and substandard quality audits, demonstrating enough firm level quality initiatives to have an environment capable of achieving quality audits; however, without enough engagement level effectiveness to consistently execute with acceptable quality.

***Aggregated engagement level statistics*** - Engagement level audit quality indicators can be built for use in two dimensions; scalability and comparability. In order to be scalable the indicators need to aggregate so that engagements level information can be combined across relevantly comparable engagements. Amounts such as percentage of partner planning hours can be aggregated for relevantly similar audits by office, partner, industry, geography and analyzed for quality indicators.

***Ineffectiveness of firm level controls*** – Engagement level audit quality failures typically indicate that multiple levels of controls and related monitoring did not exist or failed to indicate elevated risks. These failures should be analyzed to identify indicators that failed to detect both broad quality policy ineffectiveness and specific engagement level issues.

***Monitored operational controls beneficial to timely detection*** – Many audit quality issues detected by firms require additional unplanned remediation work to be performed by audit teams. Generally, the more timely the detection the less remediation effort required to address the increased risk. Unplanned remediation work is beneficial to correct known issues but can be detrimental as resources may be reallocated from other work. Firms and Engagement teams must experience tangible benefits of quality monitoring to achieve widespread compliance by audit teams. Audit quality measures designed as beneficial operational controls which can reduce unplanned rework are much more likely to achieve effectiveness.

### **The Quality Continuum**

Quality is a continuum with failure at one end and near perfection on the other. A paradox in audit quality assessment is that emphasizes failure prevention and perceives working to achieve near perfection as too costly. This perception flies in the face of examples we typically see in airline flight and manufacturing industries. In those industries near perfection is actually less expensive and easier to consistently maintain. Closer to the accounting world, the standards used on management's financial reporting control quality of Sarbanes-Oxley are far more exacting and have proved significantly more effective than the current audit quality control practices of the audit firms.

We firmly believe that the audit firm quality standards could be significantly improved and yield more cost effective results if the current quality best practices from other industries are implemented. It is ironic that the same audit firms that produce quality improvement education materials, consult on quality improvement, and test to determine the existence of material weaknesses in quality controls seem to struggle overcoming quality issues in their own work.

The focus of improvement efforts needs to be on sustained improvement in quality controls because it is almost impossible to achieve anything less and avoid occasional catastrophic failures. Interestingly, achieving the near perfection quality levels will cost less to achieve than the savings from reductions in the overall cost of audits, audit quality monitoring, and insurance, which combined are significantly less than the cost incurred from a single catastrophic failure.

### **Focus on Audit Process Indicators**

The audit process has milestones and metrics, (herein “*performance measures*”) which can be used to determine whether the audit is being performed as desired and provide a warning of potential audit quality issues. Because audits can vary in how they are completed, judgment can be used to determine the selection of specific *performance measures* for each engagement. Once selected the adherence to these *performance measures* can be very indicative if the audit is being performed within expectations and whether remedial actions should be considered.

The engagement specific milestones and metrics should be selected and performance criteria set as part of the engagement planning and can include milestones such as planning completion date, interim work review completion date, and metrics such as percentage of planned audit hours incurred in planning phase, and percentage of partner or specialist planned hours incurred prior to commencement of year end fieldwork.

Audit engagement *performance measures* would be set by the engagement teams in accordance with firm policy, **communicated to the audit committee**, and then monitored for both significant deviations and excessive numbers of deviations that would trigger a quality review and remediation prior to completion of the engagement. This type of real-time, committed, and transparent monitoring of performance versus plan is critical to any quality control program.

Although we firmly believe that the focus of the criteria should be set towards achieving a near perfect audit, discretion of the selected levels of tolerance can be left to the individual firms as long as they are recorded and transparent to clients and regulators. Ultimately, it is the cumulative effect of engagement level tolerances and firm-wide policies which will determine the overall quality.

We do firmly believe that audit firms are fully capable of achieving consistent quality levels that are in excess of what it would take to earn PCAOB inspections which are completely clear of material weaknesses and significant deficiencies.

### **Responses to Selected Concept Release Questions**

We have repeated the selected PCAOB concept release questions in italics below and provided our responses directly below each italicized question.

***Question 1.** Is increasing knowledge about, and use of, the audit quality indicators discussed in this release likely to provide insights about how to evaluate, and ultimately improve, audit quality? If so, why? If not, why not?*

Audit Quality Indicators (“AQIs”) are likely to provide insights as long as it is possible to use the data collected to drive action and make a changes in real-time. Since the majority of deficiencies in audit quality originate at the engagement level, we believe that AQIs will lead to improvements in audit quality if they are applied at that level. Further, in order to be effective at improving quality, the primary focus of the effort must be directed towards improving quality, not data aggregation. We believe that if the AQIs are used as a tool to measure performance and make changes at the audit engagement level in a real-time fashion, audit quality will be improved significantly.

***Question 2.** Are the AQI project, and some number of the 28 specific indicators described below, likely to build a strong knowledge base to enhance discussions of audits among those involved in the financial reporting process or other users of AQIs?*

Absolutely, the AQI project is very likely to build a strong knowledge base and to spark enhanced discussions. We do however believe that existing frameworks and the Sarbanes-Oxley experience should be leveraged as the basis for an AQI program. To increase audit quality, the AQI project should be viewed as a starting point and expected to evolve over time. We caution that during the evolutionary process some AQIs may become overly and unnecessarily complex. The focus should be to improve AQIs to make them more succinct rather than arduous.

***Question 3.** Can the development of audit quality indicators, as described in this release, have unintended consequences, either positive or negative, for audit committees, audit firms, investors, or audit or other regulators? What are they? Can any negative consequences be alleviated? How?*

Negative unintended consequences are generally a result of the creation of new programs without leveraging existing bases of knowledge and experience. This is why we recommend using the COSO and SOX experiences as a base for an AQI program.

***Question 4.** What is the nature of the context that those using AQIs as a basis for analysis and discussion will generally require to be able to benefit from that use? Is the information required to build that context available? Is access to the necessary contextual information feasible?*

In order to benefit from potential AQIs analysis and discussion, the relevant context needs to originate from the current engagement experience. The context may be enhanced by information from recent previous years which is both extremely relevant and easily accessible. The next most valuable context comes from relevant context. This relevance is specific to the entity which may determine that similar size is more relevant than similar geography or similar industry. Context may also be built from comparable data of relevant engagements.

**Question 5.** *Should any indicators be omitted from the list proposed in this release? Which indicators? Why?*

There are certain indicators which are too subjective to be useful. That said, if the indicator definitions are made available to the audit committees and auditors, an agreement between the parties could be made as to which AQIs are relevant to the engagement in question. We agree that there should be an initial set of indicators to start the AQI discussion and over time, we expect that this will result in an evolutionary process of the indicators. Our hope is that during the evolutionary process there will be keen focus on improving AQIs to make them more succinct simple, clear, concise, and objective.

**Question 6.** *Should any indicators be added to the list? What are they? Why? How would they be quantified?*

We noted in our previous letter (attached in Appendix B) a number of additional indicators that should be considered for inclusion. Specifically, we noted that processes in a changing world should be measured by its ability to be self-monitoring, adaptable, detective and optimizing. There is an entire section on process effectiveness missing from the AQI which should be considered for inclusion.

**Question 7.** *Which indicators are likely to be the most useful in evaluating audit quality and informing discussions of audit quality? Why? The least useful? Why?*

The indicators which are likely to be the most useful are those which are closest to the individual engagements. These are indicators at the engagement level, process quality indicators and the results of the AQIs identified and jointly agreed upon to be the most appropriate for the engagement by the audit committee and auditors.

**Question 8.** *Which indicators, including any mentioned in response to Questions 6 and 7, are in use today? How are they being used? Which ones are relatively more effective? Less effective?*

We are unaware of any indicators currently being agreed upon by both audit committees and auditors.

**Question 9.** *Definition of the Indicators.*

a) *Are the indicators clearly defined?*

For an initial project, the definitions are reasonably defined. As discussed previously, we expect that over time, the definitions will improve through the evolution of the AQI experience. It is important to note that over time, the indicators could become more subjective. With increased subjectivity, they risk becoming overly complex. Therefore, an effort should be made to ensure that indicators maintain simple, clear, concise and objective or they risk becoming useless.

**Question 10.** *Do particular indicators risk becoming too complex in operation to reflect the reality of particular audit situations?*

Most indicators are at risk for evolving into overly complex and subjective indicators over time. See our response to question 9.

**Question 11.** *Does the time lag between an audit year and the availability of information for many of the results indicators (e.g., whether a restatement has occurred) affect their value? How?*

Time lag can be remedied by maintaining indicators real-time during the performance of the audit. This should be done by the auditors on every engagement so that when control deviations occur, there is immediate action that is taken to remediate the deficiency. Aggregate numbers and large volumes of information will have a minimal improvement in audit quality overall. To have a significant audit quality impact, we strongly encourage the focus to be on the engagement level.

**Question 13.** *Are data available for each of the indicators? To what extent, specifically, is the data already broken out in audit firms' operating systems?*

Most of the data is currently available at the engagement level and is logged and tracked as part of the standard audit process. Data for the indicators should be gathered from the engagement level and accumulated in a bottom up rather than a top down approach.

**Question 14.** *The indicators operate at the engagement level, the firm level, or in most cases both.*

In most cases, the base of the indicator is at the engagement level and the AQI results of the inputs are from the engagement level.

*a) How should "engagement level" be defined in the case of a global audit in which work is referred to one or more "other auditors" (whether or not the firm or firms involved are part of the engagement firm's global network)? Who should make that determination?*

Audits are uniquely customized, so "Engagement level" should be determined on a client by client basis. It is understood that some engagements will have cross over where certain offices perform work at the direction of other offices.

**Question 21.** *In what ways should the various indicators be evaluated or field-tested?*

The entire program should be field tested and should be implemented using an Agile methodology with a focus on continuous improvement. The best innovations will come from allowing the firms and clients to spark innovation from a structured competition. The PCAOB's role should be one of increasing the expectations, standardizing certain areas which do not work themselves out and providing visibility and audit to the compliance with the programs.

**Question 22.** *For what class or classes of users would AQIs be most valuable? Would some AQIs be more valuable than others to various classes of users?*

The most valued classes of users should be the Companies and auditors. A well-designed win-win project will increase quality and reduce cost. It will add value to the company and reduce risk from the auditor. The public and investors will benefit if the audit quality rises, the boards are more actively involved and when efficiency and effectiveness are improved.

**Question 23.** *Are there one or more groups, in addition to audit committees, investors, audit firms, and the Board and other regulators, that the Board should consider to be primary users of audit quality indicators? If so, what are they? Does their need for the indicators, in each case, differ from those of other primary users?*

The Board and the firms will be the primary users as they directly will drive implementation of greater quality.

**Question 24.** *Does the discussion of the uses of the indicators identify all likely uses? If not, what other uses should be considered?*

We believe that the primary purpose of the information should be to increase the quality of audits. Sharing of information beyond that purpose could have unintended consequence. While that may be considered as part of a later phase, firms and their clients should be heavily considered in the decision to release information.

**Question 25.** *How important to the usefulness of the indicators by audit committees and other users is AQI engagement-level data? AQI firm-level data for the audit engagement firm?*

The value of the program lies in its usefulness. The audit committee's primary responsibility is the quality of that company's audit. The best information and context for an audit committee is engagement level information. This level of data is directly actionable and will yield the greatest direct benefit. Cumulative information at the office, firm, and industry levels may also be useful, but is secondary in importance and ability to directly improve the quality of an audit.

**Question 26.** *To what extent do audit committees already receive AQI-like information from their audit firms? What are the most significant gaps in the information they receive compared to the information that could be contained in the potential AQIs?*

The Companies rarely receive any running annual data towards the performance or quality of their audits. Generally, each audit is treated as a separate event and time-based information is rarely emphasized.

**Question 27.** *To what extent would engagement-level AQIs be useful to investors? AQI firm-level data for the engagement firm? What AQIs would be most useful? Why?*

Investor usefulness should be secondary and we question the emphasis on this matter as probably introducing conflicting priorities. The greatest benefit to an investor should be the improvement of audit quality. If the quality of the audit is increased to a high level, the investor should not be provided information at the engagement level, and firm information can be used by the firms for marketing, but at the firm's discretion.

The goal of this exercise should be audit quality. We support whatever needs to be done to improve audit quality, but note that this exercise should not be viewed as a freedom of information exercise. The firms should not have more information made public than what is directly beneficial for the audit quality. We strongly encourage that the scope and objective of the exercise be focused and limited to information which would improve the quality of audits, which is already an expansive scope.

**Question 28.** *Should engagement level AQI data be made public in whole or part? Should firm level AQI data be made public in whole or part?*

Please see the note above in response to question 27 and we believe that scope should start smaller and more focused. It can always be expanded based on evidence.

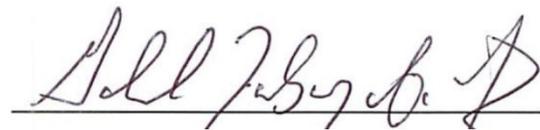
**Question 29.** *How important to the usefulness of the indicators by, audit committees, audit firms, investors the Board and other regulators, and others is the public availability of firm-wide AQI data for the audit firm that performs a particular engagement? How important is the public availability of AQI data for other audit firms of comparable size?*

Please note our answers above. Public exposure should be limited to information useful to improving the quality of audits, if deemed appropriate, necessary and based on evidence. We are not opposed to public visibility nor trial efforts of such; however, that should not be in the initial starting program. Divisive issues such as these tend to delay and divert attention from program efforts which would be more effective.

**Question 30.** *To what extent would firm-level data be more useful, for all or some indicators, if it were broken out in industry categories?*

The data should begin at engagement level (as much as possible) and then it can be aggregated into many different groups and levels with minimal effort. Breaking down data is much more time-consuming, less flexible and generally lower quality.

We appreciate the opportunity to contribute to the discussion and provide constructive feedback.

A handwritten signature in black ink, appearing to read 'Gabe Zubizarreta', is written over a horizontal line.

Gabe Zubizarreta, CPA  
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# **Silicon Valley Accountants**

## **Appendix A**

Original Response:

PCAOB Audit Quality Indicator Response to  
Briefing Paper: Meeting Date May 15, 2013

October 15, 2013

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

Re: PCAOB Audit Quality Indicator; Response to Briefing Paper; Meeting Date May 15, 2013

October 15, 2013

Dear Public Company Accounting Oversight Board:

Initially, we must begin by acknowledging the quality of the overall document which was prepared by the PCAOB. The document and approach are clear, concise and well-conceived.

Our response is intended to enhance and extend the work. The following explains the rationale for our response and shows how we incorporated that response into the feedback form.

### **Response format in Feedback Form**

We attempted to include the full effect of our response within the framework of the Feedback form format. That said, we did include some additional information in context as follows:

### **Evaluation of Defined Audit Quality Indicators**

Each indicator is evaluated in the columns provided; however, in certain instances modified indicators are proposed in the optional comments column and a second usefulness rating of the proposed modified indicator is included in the related usefulness ranking column.

### **Additional Indicator Rows**

Two types of additional rows were inserted:

Commentary rows – These commentaries were either related to the general sections of specific rows and are referenced in the first column of the new row.

Additional Indicators – Completely new indicators were added and include references in the first column to the section which they would append. The commentary in these rows attempts to explain their rationale.

## **Key Issue Discussion**

### **Unit of measure consideration**

Audit Quality measures at all levels of unit of measure are important. Our response is built on a premise that the base level is the audit engagement unit of measure for four reasons;

- 1) failure variations occur at the engagement level ,
- 2) higher level unit measures can be built from properly aggregated engagement level statistics one proposed aggregation is at the industry level ,
- 3) engagement level failure indicates ineffectiveness of firm level controls, and
- 4) engagement level process quality performance indicators can serve as monitored operational controls beneficial to timely detection of quality issues requiring performance adjustments.

***We expect the most common and vociferous response to assert that aggregation at the engagement level is impractical.***

***Failure variations*** - Audit quality varies significantly within the same firm. Based on the results of the PCAOB’s ongoing inspections, there is ample evidence of this wide variation of audit quality at each of the larger firms. Most firms perform both acceptable quality and substandard quality audits, demonstrating enough firm level quality initiatives to have an environment capable of achieving quality audit; however, without enough engagement level effectiveness to consistently execute with acceptable quality.

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## The Quality Continuum

Quality is a continuum with failure at one end and near perfection on the other. A paradox in audit quality assessment is that emphasizes failure prevention and perceives working to achieve near perfection as too costly. This perception flies in the face of examples we typically see in airline flight and manufacturing industries. In those industries near perfection is actually less expensive and easier to consistently maintain. Closer to the accounting world, the standards used on management's financial reporting control quality with the advent of Sarbanes-Oxley are far more exacting and have proved significantly more effective than the current audit quality control practices of the audit firms.

We firmly believe that the audit firm quality standards could be significantly improved and yield more cost effective results if the current quality best practices from other industries are implemented. It is ironic that the same audit firms that produce quality improvement materials and consulting regarding just those very principles for their clients; and that those same firms test and determine the existence of the very material weaknesses in quality controls that they seem to struggle overcoming in their own work.

The focus of improvement efforts needs to be on sustained achievement of the near perfection performance in quality controls because it is almost impossible to achieve anything less and avoid occasional catastrophic failures. Interestingly, achieving the near perfection quality levels will cost less to achieve than the savings from reductions in the overall cost of audits, audit quality monitoring, and insurance, which combined are significantly less than the cost incurred from a single catastrophic failure.

## Focus on Audit Process Indicators

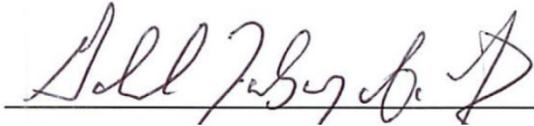
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We appreciate the opportunity to contribute to the discussion and provide constructive feedback.

Regards,

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# Silicon Valley Accountants

## Appendix B

Original Response:  
Audit Quality Indicator Evaluation Form  
October 15, 2013

**Introduction**

The PCAOB staff is conducting a survey of various stakeholders related to the priority project on audit quality indicators. In order to collect your input in an organized manner, we ask that you complete the following form.

**Questions and Instructions**

- 1) Please write your name in the space below. Your response is for internal purposes only and will be aggregated with other responses for presentation purposes. You will remain anonymous and your name will not be displayed and/or associated with any public documents.

Gabriel Zubizarreta
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- 2) Which category best represents your current professional focus?

<b>THOUGHT-LEADER CATEGORY</b>	
<b>Issuer</b>	
<b>Investor or Investor Advocate</b>	
<b>Auditor</b>	<b>X</b>
<b>Audit Committee Member</b>	
<b>Academic</b>	
<b>Other</b>	<b>X</b>

3) Please rank each of the audit quality indicators listed in the briefing memo on a 1 to 5 scale, with 1 being not useful to audit committees and 5 being useful. Refer to Appendix II in the briefing memo for further explanation and context around each of the individual audit quality indicators reflected below. Please evaluate each audit quality indicator independent of your evaluation of other audit quality indicators. That is, we are not asking you to grade metrics on a bell curve. If you strongly agree or disagree on the usefulness of a particular audit quality indicator, we encourage you to provide comments next to each audit quality indicator.

NO.	AUDIT QUALITY INDICATOR	USEFULNESS RANKING SCALE 1 = not useful 5 = useful	OPTIONAL COMMENTS
<b>OPERATIONAL INPUTS (PEOPLE)</b>			
1	Ratio of partners to staff	As-Is: 1 Opt: 4	Engagement level Improvements: Ratio of Partner Hours to Manager hours to Senior/Staff
2	Partner and staff utilization percentages / workloads	As-Is / Opt 1 / 4	Percentage of engagement hours incurred in weeks where team member utilization exceeds 100% by Staff/Senior, Manager, Partner levels
3	Chargeable hours per professional	As-Is / Opt 2 / 4	Percentage of engagement fees incurred to fees collected.
4	Excessive turnover and transfers of audit personnel	As-Is / Opt 1 / 4	Percentage of engagement hours performed by team members with less than two years of experience on the engagement by Staff/Senior, Manager, Partner levels
5	Average years of experience / headcount composition	As-Is / Opt 3 / 5	Percentage of engagement hours performed by team members with less than two year of experience at the firm by Staff/Senior, Manager, Partner levels

NO.	AUDIT QUALITY INDICATOR	USEFULNESS RANKING SCALE 1 = not useful 5 = useful	OPTIONAL COMMENTS
6	Industry expertise and proficiency	As-Is / Opt 1 / 4	Percentage of engagement hours performed by team members with less than two years of experience in the industry by Staff/Senior, Manager, Partner levels
7	Training hours per audit professional	5	Percentage of training hours in Accounting and Auditing courses
8	Number of accounting and auditing consultations	As-Is / Opt 1 / 4	Percentage of engagement hours of accounting and audit consultation
9	Percentage of work outsourced to service centers	As-Is / Opt 3 / 4	Percentage of engagement hours performed by team members in service centers.
10	Technical resource FTEs	As-Is / Opt 1 / 4	Percentage of engagement hours performed by technical resources on the engagement.
11	Specialist hours as a percentage of overall engagement hours	5	
12	Fly-in partners and managers involved in the audit	As-Is / Opt 2 / 4	Percentage of engagement hours performed by "Fly-in" team members by Staff/Senior, Manager, Partner levels

NO.	AUDIT QUALITY INDICATOR	USEFULNESS RANKING SCALE 1 = not useful 5 = useful	OPTIONAL COMMENTS
13	Partner, manager, engagement quality reviewer hours and timing relative to total audit effort	5	Percent of quality review hours spent prior to yearend fieldwork and prior to earnings release, if any.
<b>PROCESSES</b>			
1	Number and substance of firm leadership communications on audit quality and investors' interests	2	
2	Anonymous survey of firm personnel about the firm's tone at the top, hiring success, training, supervision, and to what extent a firm rewards standing up to client pressure	As-Is / Opt 3 / 5	Internally or external shared results of audit quality measures from anonymous surveys regarding AQI's
3	Metrics related to independence, testing, and compliance	?? – too vague	
4	Nature and quantity of firm proposals and marketing materials with respect to audit quality and independence	?? – too vague	
5	Number and nature of internal quality review findings	As-Is / Opt 2 / 5	Number and nature of internal quality review findings recurring for a consecutive year. Comparative analysis on repeating findings, their initial remediation plan and status
6	Number and nature of PCAOB inspection findings	As-Is / Opt 2 / 5	Number and nature of PCAOB inspection findings recurring for a consecutive year

NO.	AUDIT QUALITY INDICATOR	USEFULNESS RANKING SCALE 1 = not useful 5 = useful	OPTIONAL COMMENTS
7	Average compensation at partner and manager level to ensure adequate financial incentive and resources	As-Is / Opt 2 / 5	Percentage of partner and manager compensation tied directly to audit quality results measures such as inspection results, restatements, and evaluations
8	Compensation trends of prematurely-rotated partners	1	
9	Relative emphasis on technical competence and fortitude in the partner and manager evaluation and compensation processes	As-Is / Opt 2 / 5	Percentage of partner manager compensation tied directly to audit quality input measures, such as training, planning, and teaching
10	Credentials of new hires and recruiting: academic achievement; best companies to work for rankings; compensation levels	4	Number of training hours actually delivered prior to initial engagement
11	Technical competency testing	As-Is / Opt vague / 4	Percentage of audit partner hours billed to hours spent on teaching technical accounting and auditing issues.
12	Leverage ratio of audit staff to partners	As-Is / Opt vague / 4	Too broad. Ratio of audit hours billed by audit partner / manager / senior-staff levels.
13	Number and size of auditor resignations	As-Is / Opt 3 / 4	Percentage of audit hours incurred on resigned clients

NO.	AUDIT QUALITY INDICATOR	USEFULNESS RANKING SCALE 1 = not useful 5 = useful	OPTIONAL COMMENTS
14	Percentage of clients assessed as high risk	As-Is / Opt 2 / 4	Percentage of audit hours incurred spent on high risk clients, new clients, and lead audit partners with less than 2 years on the account
15	Level of firm investment in infrastructure supporting quality auditing	As-Is / Opt 2 / 4	Percentage of audit revenue dollars collected spent on audit quality infrastructure, training and audit defense.
<b>RESULTS</b>			
1	Frequency and market impact of financial statement restatements for errors	As-Is / Opt 2 / 4	Number adjustments and average absolute Percentage of Revenue of restated amounts. Number of passed adjustments and % of revenue
2	Number and percentage of unqualified ICFR opinions with material errors in the following year	5	
3	Number of material weaknesses cited in conjunction with material errors	As-Is / Opt 4 / 5	Avg. Number of years weaknesses existed undiscovered prior to material error.
4	Number of audit reports including a going concern opinion which did not have a subsequent bankruptcy	1	Not very meaningful.
5	Number of audit reports lacking a going concern opinion which had a subsequent bankruptcy	5	Extremely indicative and useful.

NO.	AUDIT QUALITY INDICATOR	USEFULNESS RANKING SCALE 1 = not useful 5 = useful	OPTIONAL COMMENTS
6	Surveys of audit committees about the quality of communications from the auditor	5	As long as quality is broken down into timeliness, completeness and objective
7	Trends in practice protection costs	3	
8	Trends in the frequency, magnitude, and results of litigation against auditors	3	
9	Frequency, nature, and market impact of reported frauds	As-Is / Opt 1 / 4	Number of fraud issues by severity detected per 1000 audit hours.
10	Number and nature of internal quality review findings	As-Is / Opt 3 / 4	Number of new issues, recurring issues, and resolved issues from quality review findings.
11	Number and nature of PCAOB inspection findings	5	
12	Trends in PCAOB and SEC enforcement actions	As-Is / Opt 2 / 4	Very Broad – Would need to understand actionable outcome intention. Consider number of issues noted in two consecutive years.

- 4) The briefing memo listed about 40 candidates for audit quality indicators. That list may not be complete. Which additional audit quality indicators, if any, do you suggest the PCAOB consider? For each audit quality indicator, please describe why you would find it helpful.

NO.	ADDITIONAL AUDIT QUALITY INDICATOR	RATIONALE
O	Operational general comments	If the engagement level inputs are tracked then they can be aggregated by partner, geography, industry etc. If the unit of measure is percentage of audit hours many size related issues can be normalized where appropriate. Improvements are to increase comparability and correlation potential.
O3, P5, P6	Recurring Issues	The occurrence of single year issues clouds the significant quality issue which is the ability to correct, improve and resolve. Focus should highlight recurring issues which speak to Framework Operational Issues.
P	General Process Issues	Process in a changing world should be measured by its ability to be self-monitoring, adaptable, detective and optimizing. There is a whole section on process effectiveness missing with metrics such as those added below.
P16	Percentage of audit engagement hours with planning completed and communicated within 30 days of agreed optimal date	Audit Planning is a base element of quality. The customer should have an agreed upon expectation that the audit will be planned in an optimal manner. The firm should track which audits were not planned within this expectation and planning remediation should be considered.
P17	Percentage of audit engagement hours with interim work completed and signed of within 30 days of agreed optimal date	Interim work is another base element of quality. The customer should have an agreed upon expectation as to the scope and quality of the interim work. Audits with unplanned deviations of interim work should be monitored communicated and considered for planning remediation.
P18	Percentage of planned audit engagement hours not within 90% of actual hours.	Adequate planning and execution according to plan should lead to hours incurred within 90% of expectations. Deviations outside this should be monitored, communicated and considered for remediation.

NO.	ADDITIONAL AUDIT QUALITY INDICATOR	RATIONALE
P19	Percentage of audits completed within targeted percentages of AQI metrics	Each engagement should have AQI metrics as determined by the firm with similar objectives as discussed herein. The firm should agree with the customer to which metrics will be monitored and deviations communicated. Agreed AQI deviations would have firm responses communicated to the customer.
P20	Percentage of AQI metrics missed, timely remediated, and untimely remediated	To the extent that the firm's internal metrics are not achieved then there should be a timely quality control response. For example if the "Fly-In partner" percentage is exceeded, then additional reviews or communication would be performed
P21	Aggregate percentage of audit hours completed with untimely remediated items.	The goal would be that AQI measures are targeted and monitored, and responded to on a timely basis. Aggregate hours of audits without timely responses would be tracked and reported
R	Results general	Results are a function of the inputs and the process. As these are detective in nature and indicative of issues after the fact, they are important to develop and evolve continuously and based on the changes produced by the input and process. As quality improves the deviations monitored will be less failure oriented and more refined towards 99+% excellence of achievements.
Gen	Overall General	The audit quality efforts by the PCAOB should be commended by companies, auditors, investors, regulators and the public at large. There is a huge perception issue which the PCAOB has not addressed head on. I appreciate the commissions and staff's efforts. The volume of my input is in no way critical of the efforts which are excellent; they are merely my way to attempt to contribute.

- 5) The briefing memo discussed alternative “units of account” for audit quality indicators (i.e., audit quality indicators could relate to the engagement, office, affiliate firm, or global firm level). What observations do you have about the appropriate “unit of account” for audit quality indicators?

Audit quality issues start at the engagement level. There would be no discussion if all audit engagements were performed with exceptional quality.

It is absolutely clear that exceptionally well performed audits can and do currently exist at firms. Unfortunately, poorly performed audits also co-exist at those same firms. It is at the engagement level where even strong firm and office initiatives break down. There is vast effectiveness variability at the engagement level.

Superior quality is the result of a combination of all units of measure, but it is critical that the engagement level units be prioritized. Additionally, many firm level indicators can be obtained from aggregating properly collected engagement level information.

Excellence in audit effectiveness is not a theoretical goal; it is achieved on an economically viable basis every day. It will hopefully be extended and institutionalized by efforts such as these.

Because of the variability of each client audit engagement and disproportionate influence of the engagement partners and managers the most critical unit of measure is at the engagement level.

- 6) The briefing memo offered a possible definition of audit quality. Do you find the definition acceptable? If not, why not and how would you improve it?

- A) The ability to effectively plan and communicate a set of procedures to perform independent and reliable audits to the audit committee regarding:
1. financial statements, including related disclosures (includes going concern);
  2. assurance about internal control; and
  3. financial reporting effectiveness.
- B) The ability to execute and document the aforementioned procedures to professional standards, while timely communicating and evaluating any changes, results and issues noted during those procedures, and determining the correct responsive actions.
- C) The ability to communicate and summarize significant issues noted, and form an overall conclusion regarding each of the items enumerated above.

- 7) The briefing memo offered a possible framework for considering audit quality. Do you find the framework acceptable? If not, why not and how would you improve it?

The framework is one of the best summarizations I have seen to date. It is comprehensive and very descriptive.

Other emphasis and enhancement issues:

- 1) Understanding of the specific business entity. – One of the most critical Audit Quality components is the understanding of the industry and the business about to be audited. If there are no input or process measures then this critical component will be missed. Suggest percentage of engagement hours spent on understanding of business before the audit planning by level. Additionally, percentage of hours incurred on client related education of team understanding prior to interim work (including the consultation of industry experts for team education prior to planning).
- 2) An audit is a process- As mentioned above in-line process performance measures are critical to quality achievement of any process. This has been under addressed in the application of the framework as it is there. If there is a customer view then there must be a business management view.
- 3) Continuous Improvement – Given the changing nature of the environment, which is not addressed, there must be a focus on continuous improvement to keep the audit approach focused on the changing risks. Suggest a monitoring of the process improvement hours as a percentage of total hours.
- 4) Risk based model issues – As an audit can be performed in two differing approaches risk-based or substantive there are some issues which become critical in the risk based model. Primarily, understanding the reliance in risk based auditing of the following:
  - a. Monitoring for changes which affect risk allocation assumptions
  - b. Non-prescriptive approaches to exceptions and deviations and effect on risk assumptions
  - c. Understanding of the enterprise, environment and risks to properly employ risk based auditing
- 5) Fraud – There is an abundance of undetected fraud according to statistics and actual discoveries. Auditors have a historically low incidence of finding frauds that when discovered were not well hidden or difficult to detect. Although detecting fraud is not the objective of an audit it could be a sound indicator of audit quality. Even without specifically targeting fraud a well-designed audit could be more efficient and discover more fraud
- 6) Efficiency and effectiveness – A better quality audit is actually less expensive and more effective. Poor audit quality is more expensive for the customer, auditor, investor and society at large.