THE PCAOB:  
ONE SAG MEMBER’S PERSPECTIVE  

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Highlights

DISCLAIMER! Views expressed are my own and should not be attributed to nor assumed endorsed by either the PCAOB or rest of SAG membership.

1. Overview and PCAOB History

2. Standing Advisory Group: Role and Function

3. Update on PCAOB Standard Setting Agenda

4. Concluding Remarks
PCAOB History...1

- Jan. 8, 2003: Board Member Charles D. Niemeier is named Acting Chairman
- July 30, 2002: Sarbanes-Oxley Act of 2002 is enacted, establishing the PCAOB*

(* Don Kirk testimony re FASB/SEC relationship)
PCAOB History...2

- June 21, 2004  First Standing Advisory Group* meeting
- April 25, 2003  PCAOB receives SEC determination, as required by the Sarbanes-Oxley Act, that it is appropriately organized
- April 16, 2003  Board adopts AICPA standards as Interim Auditing Standards
- Jan. 9, 2003  First open board meeting

*Note: SAG advises on audit standard setting only
SAG MEETING TOPICS

June 2014
October 2014
November 2014
June 2014 SAG meeting

- Initiatives to improve audit quality using root cause analysis (RCA), audit quality indicators (AQI), and (firm) quality control standards
- Cybersecurity issues and implications
- New RevRec FASB/IASB standard, and financial reporting and auditing implications
- New FASB Going Concern standard
October 2014 Special Meeting

Auditing Accounting Estimates and Fair Values

- Biggest concern was over characterization of “measurement uncertainty”
- Should auditors be asked to formally “audit” every material disclosure, even if, sometimes, their underlying measurement uncertainty makes it impossible to do so?
November 2014 SAG meeting

- Fraud detection, including auditor incentives to detect fraud, behavior related considerations, lessons learned from other disciplines, and auditors’ knowledge and skills regarding fraud detection.

- RevRec FASB/IASB standard, and financial reporting and auditing implications

- PCAOB staff summary of “Auditing Accounting Estimates and FVM” consultation paper comments received
Recent PCAOB Developments…1

- PCAOB key considerations/concerns:
  - Conducting its 2014 inspection cycle with focus on:
    - Auditor’s identification and assessment of the risk of material misstatement in accordance with PCAOB standards
    - Implementation of PCAOB AS No. 16, *Communications with Audit Committees*
    - Root cause analysis of inspection deficiencies
  - Continued efforts to develop cross-border arrangements to facilitate its inspections outside the United States. PCAOB oversees 230 non-U.S. based audit firms in 50 foreign jurisdictions
Recent PCAOB Developments…2

- PCAOB key considerations/concerns (continued)

  - Continuing interim program to inspect audits of brokers and dealers: concerns over computation of customer reserves and net capital, testing of revenue, testing RPTs, identification of RMM due to fraud, and independence, esp. when bookkeeping services are provided to audit client

  - Communication of inspection findings with audit committees
Standard Setting Agenda

Board Actions expected by March 2015:

• The Auditor’s Reporting Model
  • Reproduced

• Framework for Reorganization of PCAOB Auditing Standards
  • Similar to FASB “Codification” project—adoption expected

• Staff consultation papers:
  • Guidance for Auditors of Broker Dealers (June 2014)
  • Matters Related to Auditing Revenue (Sept 2014)
  • Matters Related to Auditors’ Going Concern Opinion (Sept 2014)
Revenue Recognition Standard

- Principles based, but nevertheless complex 700-page standard, requiring much financial reporting and auditor judgments

- Given absence of precedent, auditors will be greatly challenged in initial years of application

- Although effective periods not until 2016-2017, IASB allows early adoption that may happen in 2015 itself

- Need for separate auditing standard on RevRec?
RevRec and Auditing Revenue

- Evaluating revenue recognition from contractual arrangements
- Auditing gross versus net presentation of revenue
- Revenue recognition disclosures, and whether recognized in correct period
- RMM due to revenue–related fraud
- Testing and evaluating controls over revenue, esp. for multiple locations
- Substantive testing and sampling procedures
Detecting F.S. Fraud

- Auditor professional skepticism (esp. confirmation bias and selective attention)
- Management integrity, incentives, and opportunity
- Types of fraud to be defined by PCAOB?
- Improved learning curriculum for auditors focused on assessment of fraud risk
- Use of data analytics
- Leveraging internal audit function
- Financial reporting supply chain, ecology
Concluding Remarks

- Tremendous opportunity for academics to contribute to public policy and standard setting
- Now international perspectives exist through representation on SAG (e.g., IASB, IAASB)
- PCAOB has academic fellows program and invites researchers to make presentations
- PCAOB scholarship for students available
- Auditing profession has been made stronger as a result, and audit effectiveness has been improved globally (e.g., actions re Satyam fraud)