

January 3, 2014

The Honorable Mary Jo White  
Chair  
United States Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Dear Chair White:

I am pleased to transmit to you a summary of the Public Company Accounting Oversight Board's most recent performance review, titled The PCAOB's Procedures to Evaluate Firms' Remediation Procedures. The Board's Office of Internal Oversight and Performance Assurance (IOPA) conducted this performance review. The Board formed IOPA to provide the Board, the Securities and Exchange Commission, and others assurance that the PCAOB is achieving the objectives of Title I of the Sarbanes-Oxley Act in an effective manner.

IOPA undertook this review in 2013 to determine whether the PCAOB's Division of Registration and Inspections (DRI) had an adequate plan for concluding its evaluation of certain aged remediation submissions. The PCAOB Board and staff had made action on those submissions – and more generally improving the timeliness of remediation determinations – a priority, as reflected in the PCAOB's recent strategic plans and my Chairman's Messages accompanying those plans. I am pleased that IOPA found that an adequate plan is in place and that significant progress was made in 2013 to reduce the older inventory and expedite action on the more recent inventory. IOPA also made recommendations intended to facilitate additional discussion regarding remediation initiatives. The Director of DRI agreed with the recommendations.

The remediation process is central to the Board's mission to improve the quality of audits for the benefit of investors. By identifying and incenting accounting firms to correct their quality control defects, the quality control remediation process holds the potential to lead firms to improve the quality of all their future audits. I am grateful for the competence and diligence of our Division of Registration and Inspections, under the leadership of its Director, Helen Munter, and with the assistance of our Office of General Counsel, in addressing these past submissions and refining our processes to achieve more expeditious evaluation of firms' remediation submissions. I am also encouraged by the Division's continuing efforts to probe deeply into the root causes of audit failures and to focus firms on addressing these issues.

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The attached summary of IOPA's report is scheduled to be posted on the PCAOB's Web site on or about January 17, 2014. You and your staff should feel free to contact me or the Director of IOPA, Peter Schleck (202-207-9085), if you have any questions or would like any additional information about the review.

Sincerely,



James R. Doty  
Chairman

Enclosure: The Public Company Accounting Oversight Board's Procedures for Evaluating Firms' Remediation Submissions (IOPA-2013-003), December 26, 2013

cc: The Honorable Luis A. Aguilar  
The Honorable Daniel M. Gallagher  
The Honorable Kara M. Stein  
The Honorable Michael S. Piwowar

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## PERFORMANCE REVIEW

### THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD'S PROCEDURES TO EVALUATE FIRMS' REMEDIATION SUBMISSIONS (IOPA-2013-003)

INTERNAL OVERSIGHT AND PERFORMANCE ASSURANCE  
December 26, 2013

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#### BACKGROUND AND OBJECTIVE

The Sarbanes-Oxley Act requires that inspection reports issued by the Public Company Accounting Oversight Board (PCAOB) be made available in appropriate detail to the public subject to the protection of certain confidential and proprietary information. The Act further specifies, however, that portions of inspection reports containing criticisms of or disclosing potential defects in the quality control systems of the firm under inspection will not be made public if those criticisms or potential defects are addressed by the firm, to the satisfaction of the Board, within 12 months of the date of the report.

Consistent with the Act's requirements, the Board established, through its Rule 4009, a framework by which a firm may submit evidence that it has satisfactorily addressed any criticisms or defects in the firm's quality control system included in the inspection report. The rule provides a process for review and evaluation of the firm's submission by the Director of Registration and Inspections. The Director then recommends to the Board whether or not the Board should determine that the firm satisfactorily addressed the criticisms or defects. The PCAOB's process calls for the Director's recommendation, and the Board's final determination, to be communicated to the firm. Under the Act, a firm may request review by the Securities and Exchange Commission (SEC) of a Board determination that the submission was unsatisfactory.

In 2006, the Board also issued a Release<sup>1/</sup> to provide information about the process for determining whether a firm has addressed quality control criticisms to the satisfaction of the Board for purposes of the Act. The Release included an overview of procedural aspects of the

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<sup>1/</sup> *The Process for Board Determinations Regarding Firms' Efforts to Address Quality Control Criticisms in Inspection Reports*, PCAOB Release No. 104-2006-077, March 21, 2006.

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process and described the Board's approach to making the substantive determination. In PCAOB shorthand, the term “remediation” refers to firms’ efforts to address quality control criticisms.

In recent years, the Office of Internal Oversight and Performance Assurance (IOPA) heard a number of concerns from Board members about a backlog of remediation submissions<sup>2/</sup> received from firms but for which determinations had not been finalized. As of late 2011, for example, the PCAOB had yet to make determinations on a number of firm submissions received more than one year earlier. For both annually- and triennially-inspected firms,<sup>3/</sup> the inventory of outstanding determinations continued to grow through 2012. Board members were concerned that long delays in issuing determinations reflected poorly on the PCAOB and had the potential to dilute the usefulness of information ultimately provided to investors. Quality control defects do not become public unless they are not addressed to the Board’s satisfaction within the 12-month period specified in the Act. If the Board is unable to make timely remediation determinations, the public availability of information regarding any un-remediated quality control defects is further delayed. The Board discussed this issue in its November 2012 *Strategic Plan*, establishing a near-term priority to improve the timeliness of remediation determinations and provide additional information on the PCAOB's remediation process.

In response to these issues and concerns, the Division of Registration and Inspections, beginning in 2011, added resources to its remediation efforts and acted to enhance related processes. IOPA conducted this review<sup>4/</sup> to determine whether the Division has an adequate plan for closing the remediation backlog.

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<sup>2/</sup> The Division defines the backlog for annual-firm remediation determinations as including those associated with the 2008 and 2009 inspections. IOPA has also included a discussion of the status of determinations associated with annual-firm reports issued in subsequent years and uses the term “inventory” when referring to all outstanding determinations. IOPA’s discussion of triennial-firm remediation includes all submissions received but not yet acted on by the Board as of October 22, 2013.

<sup>3/</sup> In general, Sarbanes-Oxley requires annual inspections for firms that regularly provide audit reports for more than 100 issuers and triennial inspections for firms that regularly provide audit reports for 100 or fewer issuers. The PCAOB’s Division of Registration and Inspections evaluates remediation submissions for most annually-inspected firms as part of its global network firm program. Remediation submissions for the remaining annually-inspected firms and all triennially-inspected firms are evaluated as part of the Division’s non-affiliated firm program.

<sup>4/</sup> This is a public summary of the report. The full report, prepared in accordance with Government Auditing Standards, has been issued to the Board. The full report includes a detailed discussion of the review objective, scope, and methodology.

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### RESULTS IN BRIEF

Using additional resources, enhanced tools, and training, the Division has worked with the Office of General Counsel (OGC) and the Board to reduce the inventory of outstanding remediation determinations for both annually- and triennially-inspected firms. Results to date suggest the Division's initiatives have been effective and appear adequate to eliminate the backlog and further reduce the inventories of outstanding determinations in 2014. Sustained effort will nevertheless be required to achieve this outcome and ensure that the Board is able to act on future remediation submissions in a manner that provides timely and relevant information to the public.

#### Annually-Inspected Firms

Beginning in late 2011, the Division added resources to its national office and established a team to direct, coordinate, and facilitate the evaluation of annually-inspected firms' remediation submissions. The team includes four staff members devoted to the effort full time, and one staff member whose duties include remediation as well as other assignments. In 2011 and 2012, the national office team developed new procedures for the review of remediation submissions, conducted training for inspectors in the field to aid in the evaluation of firms' corrective actions, and developed a schedule for clearing the remediation backlog. Additionally, the Division established remediation teams for six of the largest firms. These teams are integrated with and work alongside staff conducting annual inspections, but their focus is on evaluating the firms' remediation efforts.

As a result of these initiatives, the Division has made progress. As of October 2012, the Division had submitted recommendations to the Board on only 25 percent of the remediation submissions of the largest U.S. registered firms that made such submissions in 2010 and 2011. At the completion of our fieldwork in October 2013, however, over 80 percent had been presented to and approved by the Board. The Division expected to make recommendations on the remainder by December 2013. If the Division is able to meet that schedule, the backlog for annual-firm remediation submissions received in 2010 and 2011 will be eliminated.

The resource additions and process changes had also resulted in a more expeditious review of firms' submissions associated with 2010 inspection reports.<sup>5/</sup> As of October 2013, the Board had acted on two of those submissions based on Division recommendations, in one case less than eight months after the submission was made and in the other case ten months after the submission was made. The Division was working with OGC to finalize recommendations for the Board for all remaining annual firm submissions associated with 2010 inspection reports by the first quarter of 2014.

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Submissions based on 2010 reports were received by the PCAOB in 2012 and 2013.

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At the time of IOPA's review, the remediation periods for most 2011 inspections had not yet closed; therefore, most submissions were not yet considered final. The Director told IOPA that the structure and approach now in place should allow the Division to routinely make recommendations regarding future firm submissions to the Board within ten months after the close of the remediation period.

### Triennially-Inspected Firms

The Division also added resources, beginning in 2011, to its program for reviewing remediation submissions for triennially-inspected firms. Prior to that time, one Division staff member had primary responsibility for reviewing and evaluating all submissions for these firms. Three additional staff members were added to this effort beginning in 2011 and two more were to join in late 2013.

Since inception, the PCAOB had issued over 1,900 triennial-firm inspection reports. At the time of our review the Board had approved more than 900 remediation determinations. As of October 22, 2013, the Division had an inventory of 62 firm submissions that had been received and that were in various stages of the review process.<sup>67</sup>

Certain indicators suggested that the additional resources had helped to expedite the review process. Between October 1, 2012 and September 30, 2013, for example, the Division had reduced its average review time by 27 days, or 15 percent, compared to the previous 12-month period. Also, the 62 submissions in review represented a reduction from 89 the previous year. While 13 of the 62 were associated with inspections conducted prior to 2010, Division staff expected to forward recommendations to the Board for about half of these by late 2013 or early 2014.

### Ongoing Efforts

As the Division moves toward the elimination of the backlog and the Board's goal of more timely review of remediation submissions, Board members and others have suggested a number of related initiatives. There appears to be significant support for updating the 2006 Release to further define and communicate the Board's expectations for the remediation of quality control criticisms. Some have also suggested that the Division prepare a report, consistent with Board Rule 4010, that compiles or summarizes quality control findings and issues to date. In addition,

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<sup>67</sup> Not all triennial-firm inspection reports include quality control criticisms. With respect to reports that did include quality control criticisms, in addition to the 62 that were in review, the deadline for a remediation submission had not yet passed for another 150 submissions, and in numerous other cases the quality control criticisms were made public by operation of PCAOB rules because the firm made no remediation submission. In addition, in some cases no submissions were made and no action taken because the firm had ceased to be registered before the remediation deadline.

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SEC staff members have recommended certain changes to inspection reports that, in the SEC staff members' view, would help streamline the remediation process. The Director of Registration and Inspections expressed willingness to move forward on these projects, but preferred to keep Division staff focused on clearing the annual-firm backlog first. The Director noted that some of the same staff members currently dedicated to managing the remediation process would likely be called on to help with updating the Release or writing compilation reports.

Careful planning will be required to ensure that the Division can accommodate Board-directed changes to remediation policy or process without sacrificing the ability to avoid future backlogs. As such, we recommended that the Director meet with the Board to discuss budget and schedule implications of potential policy initiatives. The Director planned to do so in December 2013.