

August 7, 2023

Ms. Phoebe Brown
Office of the Secretary
Public Company Accounting Oversight Board
1666 K St, NW
Washington, DC 20006-2803

PCAOB Release No. 2023-0003, June 6, 2023: Amendments to PCAOB Auditing Standards related to a Company's Noncompliance with Laws and Regulations

Dear Secretary Brown and PCAOB Board Members:

Johnson Global Accountancy is pleased to submit its comments on the proposed amendments to auditing standards related to an auditor's consideration of a company's noncompliance with laws and regulations.

Johnson Global Accountancy's mission is to be the most innovative and technically excellent advisory firm at the intersection of companies, auditors, and regulators, which improves investor decision-making confidence. We serve a diverse group of audit firms ranging from single office firms to more complex regional firms and the top 20 firms. We help firms interpret, respond, and comply with global auditing and financial reporting standards and regulatory requirements, including those standards set by the PCAOB. Our team of financial reporting quality advisors helps prepare firms to perform high-quality audits using innovative tools with a shared commitment to implement effective policies, procedures, and controls. We also provide firms with integrated software and service solutions to help them comply with audit quality standards.

Overall, we support the need for investors to understand the risks of noncompliance with laws and regulations applicable to companies, whether it be risks of potential noncompliance, or known instances of noncompliance.

Since the auditor's objective is to perform procedures to determine that a company's financial statements are free of material misstatement, whether due to error or fraud, we believe it is a reasonable concept to extend the auditor's responsibility to other aspects of material misstatement, such as material misstatement of the financial statements due to noncompliance with laws and regulations.

However, we do believe that the scope of the proposed standard, and the expectations it would place on auditors, does go beyond that concept. We have addressed certain questions in the proposal at the end of our response. In addition to our comments on the specific questions, our general observations and comments include:

- 1) The proposal places an emphasis for the auditor to identify laws and regulations with which noncompliance could reasonably have a material effect on the financial statement. More clarity is needed on the phrase "could reasonably have a material effect". Our goal would be for auditors to focus their efforts on those laws and regulations that, if violated, the non-compliance would be likely to result in a material effect on the financial statements.
- 2) We noted some expectations that could pose some inconsistencies in the scope of the relevant laws and regulations subject to evaluation, for example, (i) the objective of the

auditor to identify laws and regulations with which noncompliance could reasonably have a material effect on the financial statements (paragraphs .04 and .05); and (ii) the expectations for auditors to evaluate – and communicate – noncompliance regardless of whether it is perceived to be material to the financial statements (paragraphs .07 and .12).

- 3) We believe that client management and those delegated with management responsibility including their compliance and legal experts, are best suited for determining those laws and regulations that, if violated, are susceptible to material misstatement. Our view of the distinction of roles and responsibilities of management versus the auditor is akin to those set forth in the AS 2410, *Related Parties*.
- 4) Implementation and continuous compliance with this standard would disproportionately effect NAF firms. More often than not, NAF firms will need to engage outside specialists to add to their engagement team, including attorneys and compliance experts. Further, to address audit clients in different industries that are subject to a vast array of laws and regulations, firms will need to engage a variety of different attorneys or other experts with the specialized knowledge applicable to the company subject to audit.
- 5) We recommend working with registered firms to identify a small cross-section of domestic and non-U.S. GNF and NAF firms for a pilot to gather more quantifiable data on the costs to implement in the firm and carry out in an audit, and the unique challenges posed to firms based on their size, scalability, the qualifications, expertise, costs, and availability of in-house staff versus outside experts, and the complexity and number of industries they audit that are susceptible to law or regulations that, if violated and gone undetected, may result in a material misstatement to the financial statements.

We provide our comments to certain specific questions posed in the standard as follows:

Proposal Ques #	Question	JGA Comment
7	Is the proposed requirement for auditors to identify laws and regulations applicable to the company with which noncompliance could reasonably have a material effect on the financial statements sufficiently clear? If not, why not?	The proposed requirement appears insufficiently clear. Specifically, the phrase, “could reasonably have a material effect...” could potentially require the auditor to identify all laws and regulations that could have a financial impact at some point in time for the company. More clarity is needed to focus the auditor’s efforts on those laws and regulations that, if violated, the non-compliance would be likely to result in a material effect on the financial statements.

		<p>Paragraph .06(b.) of the proposed standard includes a “catch-all” of other procedures besides those pertaining to risk assessment procedures. We believe, while the proposed standard does (e.g. in the “Note” to the paragraph) provide certain examples of other standards that would assist to inform the auditor in identifying laws and regulations with which noncompliance could have a material effect on the financial statements or alert the auditor, this note should make clear which standards to consider the results of procedures performed, rather than a catch-all approach which is difficult for auditors and their methodology to focus and direct attention to inform them on the universe of those applicable laws and regulations.</p>
8	<p>Will auditors be able to identify those laws and regulations applicable to the company with which noncompliance could reasonably have a material effect on the financial statements? If not, why not?</p>	<p>No, we believe auditors currently are not equipped for this expectation. Engagement teams may need to engage others to complement the audit engagement team’s knowledge based about macro non-compliance risks (industry, relevant regulators, legal research of new laws, revised laws since the last reporting period, competitors facing non-compliance issues, etc.) and micro non-compliance risks specific to the company. Further, firm-engaged specialists, firm-engaged compliance or legal experts may disclaim on (i) the completeness of the population of those applicable laws and regulations; or (ii) the assessment on which ones “reasonably have a material effect on the financial statements” due to their own liability risks that are changing on a regular basis, and the risks of non-compliance having a material effect is best suited for management.</p>
11	<p>Is the proposed requirement that auditors identify whether there is information indicating that</p>	<p>Our response to questions 7 and 8 are integral to our response to this question, since the clarity of the expectations under</p>

	<p>noncompliance (with those laws and regulations with which noncompliance could reasonably have a material effect on the financial statements) has or may have occurred sufficiently clear? If not, why not?</p>	<p>paragraphs .05 and .06 of the proposed standard will drive the clarity of paragraph .07.</p> <p>We are concerned about the parenthetical clause “(regardless of whether the effect of such noncompliance is perceived to be material to the financial statements”, since the applicable of materiality seems to be contradictory to paragraphs 4, 5, 6 of the proposed standard.</p> <p>We recognize that this paragraph may be intended to include requirements under paragraph .10 of the current standard. This parenthetical clause was added in the proposed standard, however, which seems to indicate that the auditor should be reacting to instances of non-compliance that is greater in scope to the relevant laws and regulations identified through the objectives and responses in paragraphs .04, .05, and .06 of the proposed standard.</p> <p>As an aside, we have the same concern of this phrase in paragraph .12 of the proposed standard with regard to communicating the matters to the audit committee (para.12(b)). This may draw unnecessary time and attention to the audit committee on matters that do not have a material effect on the financial statements. These findings are better suited by management, including internal audit, to prevent these issues from raising to the level of a material weakness in internal control or a material misstatement in the financial statements in future periods.</p>
<p>59</p>	<p>Which proposed amendments are likely to be associated with more substantial costs? Are the costs quantifiable?</p>	<p>Broadly, we believe the key objectives of the standard, specifically paragraphs .04 a.-c., will create substantial costs for firms to implement and for engagement teams to perform each reporting period.</p>

		<p>Regarding whether the costs are quantifiable, we point to the Board’s Release on the proposed standard indicating that “imposing new requirements would result in additional, potential substantial costs to auditors and the companies they audit.” While we have not had sufficient time to study implementation and application under the new standard, we recommend the PCAOB carry out a study with a cross-section of different firms (GNF, NAF, domestic and foreign) to help quantify the costs. This will help provide a more quantitative basis for determining whether the benefits outweigh the costs.</p>
<p>60</p>	<p>Is the expansion of the auditor’s responsibilities to identify information indicating noncompliance with laws and regulations has or may have occurred without regard to the effect of such noncompliance on the financial statements practical and cost effective to implement? Are small/medium firms equipped and capable of implementing these new requirements? If not, why not?</p>	<p>We believe more study would be necessary to determine whether it is practical and cost effective to implement. This could be achieved through a pilot implementation of the standard by a cross-section of firms (GNF, NAF, domestic and foreign), with information provided to the Board to inform on the merits of implementation as a significant input to the cost and benefits analysis which, at the moment, is largely qualitative.</p> <p>Based on our work with domestic and non-U.S. NAF firms, we believe that the costs to implement, including ensuring the appropriate capabilities and expertise, will disproportionately affect NAF firms. GNF firms may be able to achieve greater economies of scale and have experts in-house, and are able to spread these costs across more audits with larger fees than their smaller firm counterparts.</p> <p>More often than not, NAF firms will need to engage outside specialists to add to their engagement team, including attorneys and compliance experts. Further, to address audit clients in different industries that are subject to a vast array of laws and</p>

		regulations, firms will need to engage a variety of different attorneys or other experts with the specialized knowledge applicable to the specific engagement and their industries, operating jurisdictions, and other considerations.
62	Are there substantial costs associated with an increased need to use auditor’s specialists to assist the auditor in evaluating noncompliance that has or may have occurred as a result of the proposed requirements? If so, are the costs quantifiable? Are there any applicable means of mitigating or reducing such costs?	<p>We believe that compliance with the standard would require compliance experts: attorneys and consultants. We believe that management is better suited as understanding the universe of laws and regulations applicable to their company.</p> <p>Regarding whether the costs are quantifiable, we point to the Board’s Release on the proposed standard indicating that “imposing new requirements would result in additional, potential substantial costs to auditors and the companies they audit.” While we have not had sufficient time to study implementation and application under the new standard, we recommend the PCAOB carry out a study with a cross-section of different firms (GNF, NAF, domestic and foreign) to help quantify the costs. This will help provide a more quantitative basis for determining whether the benefits outweigh the costs.</p>

We appreciate the opportunity to provide our comments and support the PCAOB’s efforts to improve auditing standards to enhance audit quality and better protect investors . We would be pleased to discuss our comments with you at your convenience. Please direct any questions to Jackson Johnson, President and Shareholder (jjohnson@jgacpa.com) or Geoffrey Dingle, Managing Director and Shareholder (gdingle@jgacpa.com). They may be reached at (702) 848-7084.

Sincerely,



Johnson Global Accountancy