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

Re: PCAOB Rulemaking Docket Matter No. 046

Deloitte & Touche LLP ("Deloitte" or "we") appreciates the opportunity to provide comments on *A Firm's System of Quality Control and Other Proposed Amendments to PCAOB Standards, Rules, and Forms* ("the proposal") issued by the Public Company Accounting Oversight Board (the "PCAOB" or the "Board"), including the proposed QC 1000, *A Firm's System of Quality Control* ("the proposed standard" or "QC 1000").

We are pleased to see the PCAOB's thoughtful consideration of International Standard on Quality Management 1, *Quality Management for Firms that Perform Audits or Review of Financial Statements, or Other Assurance or Related Services Engagements* ("ISQM1") issued by the International Auditing and Assurance Standards Board, and the Statement on Quality Management Standards No. 1, *A Firm's System of Quality Management* issued by the American Institute of Certified Public Accountants ("AICPA").

We commend the Board for recognizing the need for, and the benefits of, alignment with these standards – benefits which include, but extend beyond, implementation cost considerations. Having a common base structure through use of identical components (e.g., Governance and Leadership, Engagement Performance, Information and Communication) and establishing the same risk-based framework of quality objectives and their relationship to quality risks and quality responses are critical factors supporting a firm's ability to operate a single, consistent Quality Control system ("QC system"), especially when that firm is subject to the standards of different standard-setting bodies, oversight by multiple regulators, or when operating in a network of firms. Adding incremental provisions to that common base - provisions that are specifically relevant to the US environment (i.e., tailoring to the US regulatory environment) - provides a structure to operationalize the proposed standard in an effective manner.

We are also supportive of the following provisions in particular, some of which extend beyond ISQM1:

- Independent oversight role – involving someone with an objective lens, and in a manner appropriate to a firm's nature and circumstances, enables firms to address this requirement so as to provide more diverse insights on the operation of the QC system
- In-process monitoring – providing real-time feedback to engagement teams enhances the quality of audit execution
- Annual written certification by firm personnel regarding familiarity and compliance with ethics requirements and the firm's ethics policies and procedures – focuses on the importance of ethics and confirming firm personnel's understanding of such responsibilities

- Monitoring work performed by firm personnel below the "substantial role" threshold as an "other auditor" – inclusive scoping of referred work based on a judgmental determination of risk and complexity is important
- Annual evaluation of the effectiveness of the firm's QC system – having a formal process will introduce additional rigor and enhance the focus on driving development of continuous improvement actions
- Annual reporting to the PCAOB – will provide a channel for confidentially sharing information with the PCAOB, to update their understanding of a firm's QC system and inform the scope of the PCAOB's future oversight activities

Notwithstanding our overall support and the positive elements of the proposal noted above, we do have concerns with the following aspects of the proposal and other observations on which we have provided more detail below:

- Differing conclusions on, and communication of, the effectiveness of a firm's QC system
- Specified annual evaluation date of November 30
- Operationalization of the proposed standard in firms of different sizes and structures
- Inclusion of "other participants" as part of the firm's QC system
- Alignment of liability and scope of laws with existing standards and rules
- Threshold for consideration of "intentional misconduct" within the definition of quality risk
- Ethics and independence matters
- External communication of performance metrics

Differing Conclusions on, and Communication of, the Effectiveness of a Firm's QC System

We believe that the difference in the nature of the conclusions on a firm's QC system between QC 1000 and ISQM1 will result in confusion for various stakeholders, including audit committees. The risk of misunderstanding is particularly acute in the "effective, except for" conclusion where, in reaching its conclusion, a firm will have to consider two different deficiency populations (i.e., all unremediated deficiencies under QC 1000 versus "severe but not pervasive" deficiencies under ISQM 1). As a result, it is possible that two different conclusions may be reached and need to be communicated simultaneously, for example to an audit committee of a dual registrant (e.g., the firm may report to the audit committee that its QC system is "effective" under ISQM 1 but "effective, except for" under QC 1000). Using a consistent evaluation framework would alleviate confusion and inconsistency in these situations and therefore would enhance comparability.

In addition, while we are supportive of communicating the conclusion of the firm's most recent annual evaluation of its QC system to audit committees, we are concerned that the additional requirement to discuss a "brief overview of remedial actions taken and to be taken" could be difficult, if not impossible, to address without disclosing to the audit committee confidential information about unremediated deficiencies that would be protected by the provisions of the Sarbanes-Oxley Act ("SOX" or "the Act"), (Section 105(b)(5)(A)). For example, in communicating remedial actions to be taken, firms may interpret the proposed standard as requiring the sharing of information about PCAOB Part II inspection comments (and related remediation) prior to the 12 months provided by SOX for addressing them before the possibility of public

disclosure, which would negate the protections afforded by law. We therefore recommend limiting the required audit committee communication to the conclusion on the firm's QC system.

Further Considerations in Arriving at the Conclusion on the Effectiveness of a Firm's QC System

In arriving at the conclusion on the effectiveness of the QC system, we are concerned that the difference in the definitions between QC 1000 and ISQM1 may also create inconsistencies. For example, the proposal indicates a presumption that every engagement deficiency is to be considered a quality control finding ("QC finding"). We believe an engagement deficiency could be an isolated instance (e.g., human error) which does not extend to the QC system as a whole. Paragraph 71 of the proposed standard already requires that firms evaluate information from engagement monitoring in determining whether QC findings exist. We believe that the firm should make a judgment based on the engagement deficiency evaluation based on facts and circumstances as to whether a QC finding exists, and therefore recommend that the proposal enable that judgment by removing the phrase "engagement deficiencies are QC findings" from the definition of QC finding.

In addition, we are concerned that the presumption implicit in the examples of major quality control deficiencies in the proposal overrides a risk-based approach and the principles-based nature of the PCAOB standards. This removes the application of judgment when evaluating the severity and pervasiveness of a quality control deficiency ("QC deficiency"). To enable firms to exercise professional judgment, similar to material weakness judgments by companies under SOX, we recommend that the circumstances included as examples be recast as 'indicators' of whether a major QC deficiency, individually or in the aggregate, might exist.

Specified Annual Evaluation Date of November 30

We are supportive of the requirement for firms to perform an annual evaluation of their QC system's effectiveness; however, we have concerns about the proposal for a prescribed evaluation date for all firms and selection of November 30 as that date. In addition to these concerns, we have a suggestion to extend the documentation completion date.

Prescribed Evaluation Date for All Firms

We believe it is essential to allow firms to select an evaluation date that aligns with their own cycle of operations, which is analogous to the SEC allowing issuers to select a year-end (or related management certification date for internal control over financial reporting) that aligns with their business cycle. During the implementation of ISQM1 by audit firms of the global Deloitte network ("the network"), the network carefully considered various evaluation date options and concluded that a date that approximates the end of each firm's fiscal year (Saturday nearest to May 31) was the most appropriate date for all audit firms in the network, considering network firms' cycle of quality control operations (including performance evaluations, budgeting, and senior leadership changes), monitoring and remediation cycle (including root cause analysis, development and testing of remedial actions implemented), as well as required or expected timing of transparency reporting in non-US jurisdictions.

November 30 as the Evaluation Date

If the PCAOB decides to select November 30 as the evaluation date for all firms, global network firms will be put in a position of performing two separate evaluations every year, having already selected a date for ISQM1. In addition to the incremental cost of two duplicative evaluations, there is a likely risk of confusion in

the marketplace arising from (1) providing differing information to external parties (through communications with audit committees - both for ISQM1 and QC 1000 - and within transparency and other reporting), and (2) situations in which different conclusions are reached under the different standards, as we described in the comment above. We do not believe this outcome would be in the public interest.

Importantly, we are also concerned about capacity of firm personnel during the months of November through February, as many with roles within the QC system also either directly perform or support audit and assurance engagements during busy season. This includes both firm personnel who are responsible for operation of quality responses within a component of a firm's QC system (e.g., Firm's Risk Assessment Process, Resources) as well as those involved in the monitoring and remediation process, who would be responsible for performing much of the work in support of the annual evaluation and reporting.

Documentation Completion Date

We recommend that the documentation completion date be no later than 45 days after the report date, instead of the same day Form QC is submitted to the PCAOB, to allow a reasonable, but not excessively long period of time after the report date for firms to assemble the required documentation .

Operationalization of the Proposed Standard in Firms of Different Sizes and Structures

We have considered the proposal in relation to the Deloitte network of member firms, which comprises individual audit firms of diverse sizes and engagement portfolios, all of which are subject to ISQM 1. In certain cases, different structures have been used to maximize sharing of quality control resources through "clustering" certain quality control roles or processes across a number of smaller firms within a geographic region. We believe these structures can enhance consistent high-quality audit execution, broadly and at the engagement level. For example, a geographical region composed of different firms that are separate legal entities in a small number of different countries may combine their activities related to independence monitoring. Having one dedicated individual with a supporting team focused on this topic might be more effective than having three separate individuals and teams spending 30 percent of their time on this topic. As written, the proposal does not seem to recognize these types of arrangements as it requires specific roles and responsibilities to be filled by "firm personnel." In our example, this would preclude anyone from outside a specific registered firm from fulfilling a key quality control role for the firm. We therefore suggest that the proposed standard acknowledge that, in addressing the most effective way of executing quality control roles and activities, different structures may exist in the operation of the QC system, and that individuals with qualified expertise necessary to fulfill quality control roles may come from outside a registered firm in certain circumstances.

Inclusion of Other Participants as Part of the Firm's QC System

We are concerned about having "other participants" form part of the firm's QC system, as stated in the objective in paragraph 5.a, and similarly referenced in other sections of the proposed standard (e.g., paragraphs 44c, 47 and 55). As defined, "other participants" include internal auditors and external specialists. Internal auditors and external specialists are not directly subject to the firm's quality control policies and procedures, and therefore the firm cannot impose responsibilities that are part of the firm's QC system. For example, paragraph 47 indicates that the firm is required to establish quality control policies and procedures related to other participants' "maintain[ing] their competence." As internal auditors and external specialists are not part of the firm, the firm would not be in a position to impose specific learning requirements on these individuals. Further, we believe that describing "other participants" as being part of

the firm's QC system may create cross-jurisdictional legal issues – for example, a requirement to obtain and evaluate information relating to the personnel of an entity located outside the US may not be possible if employment information is protected by local privacy laws. We believe other PCAOB standards sufficiently address "using the work of others" (AS 1205, *Part of the Audit Performed by Other Independent Auditors*, AS 1210, *Using the Work of an Auditor-Engaged Specialist*, AS 2605, *Consideration of the Internal Audit Function*) and include requirements to consider the competence, objectivity, and time to fulfill their responsibilities when deciding whether to use the work of others, and as a result "other participants" should be removed from the paragraphs noted above, and elsewhere in the proposal as appropriate.

Alignment of Liability and Scope of Laws with Existing Standards and Rules

Certifications

Through the certifications by senior leaders of the firm included in Form QC regarding the design and effectiveness of the QC system, it appears that the Board intends to establish a requirement that parallels the SOX certification requirement for senior executives of public companies. We acknowledge this new requirement emphasizes the importance of accountability within and for a firm's QC system overall. However, the Board's proposal does not specify the standard against which an individual could be held liable for making a certification on Form QC that is later determined to be inaccurate. It is our understanding that, for certification by senior executives under SOX, courts have decided that a SOX Section 302 certifier can be held personally liable for an inaccurate statement in a certification only if they made the statement knowing it was false or recklessly not knowing it was false.[1] We believe it would be appropriate for the Board to clarify that the same standard applies to certifications made on Form QC.

Confidentiality

The PCAOB recognizes that, to the extent that the matters discussed in Form QC touch on the inspection process, certain information in the Form QC will likely receive the protections of Section 105(b)(5)(A) of the Act, which provides that "all documents and information prepared or received by or specifically for the Board, and deliberations of the Board and its employees and agents," in connection with an inspection or investigation, "shall be confidential and privileged as an evidentiary matter."[2] However, the Board also recognizes that the certification portions of Form QC "are not subject to privilege under Section 105(b)(5)," which creates a risk of unwarranted legal exposure for registered firms, particularly where the interconnected nature of documents and information prepared or reviewed in connection with inspections and investigations will overlap in numerous ways with documents and information prepared for and relevant to the Form QC report. Given the inextricable overlaps in information and given that the Form QC will form supplemental information for the inspection process, we encourage the Board to clarify and determine that Form QC falls within the bounds of the Board's inspection authority. We believe that the legal exposure risk posed by QC 1000's required annual evaluation and reporting justifies an arrangement that permits Section 105(b)(5)(A) of the Act to apply.

In addition, the proposed standard does not appear to recognize that certain information relevant to the description of a QC deficiency might be restricted from disclosure by the operation of legal requirements such as data protection laws or blocking statutes. This would be applicable for US-based firms in situations in which a QC deficiency is identified relating to its supervision of audit work by non-US "other participants" that is subject to data privacy regulations or for firms outside of the US that may not be able to disclose

[1] SEC v. Miller, 2:17-cv-897-CBM, 2019 WL 1460615 (C.D. Cal. Feb. 6, 2019)
[2] (15 U.S.C. § 7215(b)(5)(A))

details of unremediated QC deficiencies altogether due to such regulations. We recommend that the Board clarify how firms should address a situation in which the Board's expectation concerning the thoroughness of a firm's quality control reporting might risk a firm's compliance with other laws to which it, or the information it might disclose, is subject – as well as consider the inclusion of exemptions set forth in other PCAOB forms to acknowledge that disclosure of certain information by non-US firms may not be permitted.

Threshold for Consideration of "Intentional Misconduct" within the Definition of Quality Risk

We understand the PCAOB's rationale for the specific inclusion of "intentional misconduct" within the definition of "quality risk," as we believe it is an important consideration of "what could go wrong" when identifying and assessing potential quality risks. However, we believe that it is appropriate for the definition to also address the "possibility of occurrence" of intentional misconduct when identifying and assessing quality risks. We note that the PCAOB suggests that "limiting risks of intentional misconduct to only those that have a reasonable possibility of adversely affecting the achievement of the firm's quality objectives would result in the firm concentrating its efforts on more pervasive and larger risks and not on every conceivable act of misconduct." However, we believe it is not feasible to design and implement quality responses to address every risk that has only a remote likelihood of occurring, particularly in the context of a system where the objective is to provide reasonable and not absolute assurance of achieving its stated quality objectives. Focusing on "every conceivable act of misconduct" would result in a misallocation of time and resources compared to true risk. Accordingly, we recommend revisions to the definition of quality risks as noted below.

> *.A12 Quality risks – Risks that, whether due to unintentional acts or intentional acts by firm personnel or other participants to deceive or to violate applicable professional and legal requirements, individually or in combination with other risks, have a reasonable possibility of adversely affecting the firm's achievement of one or more quality objectives if the risks were to occur, and ~~are either:~~*
>
> *~~(1) Risks that~~ have a reasonable possibility of occurring~~; or~~*
>
> *~~(2) Risks of intentional acts by firm personnel and other participants to deceive or to violate applicable professional and legal requirements~~.*

Ethics and Independence Matters

Operational Responsibility

The proposal appears to indicate that only one individual should be assigned to the roles of both ethics and independence so that operational responsibility is not inappropriately delegated. In our experience, the scope of both roles may be too great for only one person and may detract from focus on the discrete and important, but different, goals of an ethics oversight program (that firm personnel understand and act consistent with applicable ethical rules, policies, and procedures) and an independence oversight program (that firm personnel and the firm itself remain independent of their audit clients consistent with a highly complex set of rules governing relationships with those clients and their employees). We therefore suggest that the Board clarify that the final standard does not preclude a firm from assigning one person to each of the ethics and independence operational roles, both of whom should have "a direct line of communication" to the principal executive officer and be identified on Form QC.

Monthly Communication of Changes to Restricted Entities

The proposal includes detailed specified quality responses related to (1) the firm updating and communicating changes to the list of restricted entities at least monthly, and (2) firm personnel reviewing the list of restricted entities changes after they are communicated by the firm or upon the occurrence of a

qualifying event. The requirements as written may drive responses that would not be as effective as automated processes already in place at larger firms. Such automated processes more precisely address the risks by updating restricted entity information in real-time with open access by firm personnel at all times, and especially for larger firms, are likely to be far more effective than monthly communications.

We recommend that instead of prescribed quality responses, a quality objective regarding "awareness of changes in restricted entities" should be established, which would allow firms to design their quality responses in line with the technology and processes already in place.

Obtaining Independence Certifications Upon Change in Personal Circumstances

We recommend that the PCAOB remove the specified quality response to "obtain additional certifications upon changes in personal circumstances" (especially related to changes in marital status – which employers may not be permitted to require employees to disclose). Rather, the proposal should emphasize that a firm's independence certification processes and other procedures should consider timeliness in addressing the quality objective, and instead encourage firms to consider the appropriateness of obtaining periodic certifications throughout the year.

External Communication of Performance Metrics

We recommend that performance metrics subject to the quality objective in paragraph 53(e) be clarified to indicate that the metrics in scope are those related to the effectiveness of the firm's QC system or audit quality, as these align with the PCAOB's rules and standards. In addition, we suggest that "external communications" are clarified to indicate "formal" external reporting (e.g., Audit Quality Reports, Transparency Reports, communications with audit committees, and other published reports) so as to better enable effective operation of this requirement.

Other Observations

Cycle for Selecting Partners for Inspection

We recommend allowing firms to use a risk-based approach for each firm to determine an appropriate cycle for partner and engagement selection. Further, as each Deloitte registered firm operates one QC system for all engagements within that firm (as recognized in the Release to be the most efficient and effective approach for all firms), we believe this judgment should include consideration of all engagements in a partner's portfolio.

Definition of "Applicable Professional and Legal Requirements"

The definition of "applicable professional and legal requirements" includes the phrase "other applicable statutory, regulatory, and other legal requirements" which could be read broadly as a wide range of laws and regulations that do not directly bear on the conduct of audit engagements (e.g., OSHA laws), and thus would be inconsistent with the focused statutory mission of the PCAOB to oversee the audits of public companies and broker-dealers for the protection of investors. As a result, we propose that "applicable professional and legal requirements" be clarified to mean only legal requirements that directly relate to the performance of engagements under PCAOB standards or that there be reference to specific relevant legal requirements that are intended to be brought within the ambit of the rule, such as PCAOB form reporting requirements and Securities Exchange Act Section 10A.

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Amendments to Form QC

Similar to management's report and our opinion on internal control over financial reporting, we recommend that revisions to Form QC not be required for inconsequential matters (e.g., new unremediated deficiencies or changes to existing ones that would not change the conclusion reached on the effectiveness of the QC system).

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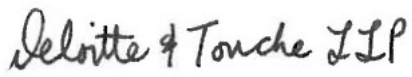
We would welcome the opportunity to engage with the Board in dialogue about these issues to provide deeper context about impacts and implications. If you have any questions, please contact Jen Haskell at 203-761-3394 or Julie Vichot at 415-783-4627.

Yours sincerely,



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