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Chair Williams Challenges Firms to Uphold the Highest Standards in Audit Quality

In keynote remarks at annual AICPA conference, Chair Williams tells firms: “Resist complacency, sharpen your focus and meet your responsibility to verify the honesty our system depends on with a vigilance that is worthy of [investors’] trust.”

Washington, DC, Dec. 12, 2022

Remarks as prepared for delivery

Public Company Accounting Oversight Board (PCAOB) Chair Erica Y. Williams delivered the following remarks today at the AICPA & CIMA Conference on Current SEC and PCAOB Developments.

Thank you, Julie [Bell Lindsay]. Thank you to the AICPA, and to all of you for being here.

Before we begin, I want to provide the usual disclaimer that the views that I express today are my own and do not necessarily reflect the views of my fellow Board Members or our talented and dedicated staff.

As he signed the Sarbanes-Oxley Act into law 20 years ago, President George W. Bush remarked, “The fundamentals of a free market – buying and selling, saving and investing – require clear rules and confidence in basic fairness. The only risks – the only fair risks – are based on honest information.”

“The American economy,” he later continued, “depends on fairness and honesty.”

As auditors, you have the incredible responsibility of verifying the honesty our system depends on.

Quality audits bolster investor confidence and help make our capital markets the envy of the world.

In the months leading up to President Bush's signing of the Sarbanes-Oxley Act, trust was betrayed, and investor confidence was eroded.

In the early 2000s, major accounting scandals from Enron to WorldCom rocked our markets. Corporations were lying about their earnings and hiding their debt, at times with the help of their auditors. And when it all came crashing down, investors lost billions and workers lost jobs and retirement savings.

People got hurt.

So, Congress took action.

Led by Senator Paul Sarbanes, a Democrat from Maryland, and Representative Michael Oxley, a Republican from Ohio, both parties came together to craft legislation that passed nearly unanimously with strong, bipartisan support.

Among other things, the law we refer to today as "SOX," established the PCAOB.

For the first time, investors had an independent audit watchdog putting their interests first. The PCAOB would set clear standards to uphold the integrity of public audits, inspect for compliance with those standards, and enforce them to help restore trust in our capital markets.

In the 20 years since, audit quality has improved. And evidence shows that increase in audit quality has boosted investor confidence in the credibility of financial reporting.

But investor confidence is not inevitable. Trust must be earned, and it must be maintained.

It takes vigilance to guard against fraud that threatens the integrity of our capital markets.

Reflecting on SOX five years after it was signed, Senator Sarbanes warned against the dangers of complacency "When things get better," he said, "companies tend to forget what happened or how serious it was at the time. Trying to maintain high standards is a difficult job."

The PCAOB is up to the task. And I challenge the auditing profession to join us in upholding high standards, which are more important today than ever.

The combined market capitalization of just 10 equity issuers today is nearly equal to the total U.S. equity market capitalization in 2002, when SOX was signed into law.

Today, the PCAOB's oversight helps to protect more than \$40 trillion in investor exposure.

Coming out of a pandemic, many companies are continuing to navigate challenges and uncertainties. Incentives for fraud are heightened.

Your vigilance must be higher.

Unfortunately, right now, the trendline is moving in the wrong direction.

Last week, we released a staff Spotlight report previewing our 2021 inspection findings. Audits with Part I.A deficiencies increased 4 percentage points in 2021 to 33% compared to 29% in 2020.

That means a third of the audits we inspected had deficiencies of such significance that PCAOB staff believe the audit firm failed to obtain sufficient appropriate audit evidence to support its opinion on the public company's financial statements or internal control over financial reporting.

At the same time, we are seeing increased comment forms for both U.S. and non-U.S. firms in our 2022 inspections. These comment forms usually result in inspection findings in our reports.

Together, these facts present a troubling warning sign.

There is no one-size-fits-all answer as to why deficiencies increased in 2021. The causes likely vary from firm to firm.

But some firms have told us that the combination of the COVID-19 pandemic, remote auditing, the Great Resignation, and the war for talent have made it difficult to maintain stable audit teams and provide training to newer hires.

As we near the end of 2022, these factors are no longer new, and no one should be caught off guard by the challenges they present.

Firms have a responsibility to design and implement solutions to restore and maintain audit quality.

I want to acknowledge that a number of firms are taking steps toward meeting these challenges, and it will take time before we see that reflected in our inspections.

At the same time, the 33% of audits with at least one Part I.A finding cannot be explained away by the pandemic.

Some of the auditing deficiencies we identified have recurred for many years, well before COVID-19 – including auditor independence, which is a critical element of an audit firm's quality control system and is essential to an audit firm's credibility with investors.

Firms must sharpen their focus and prioritize their efforts to increase audit quality and ensure investors are protected.

In order to effectively – and credibly – meet the responsibility to enforce honesty in our system, firms must enforce the highest ethical standards within your own walls.

This year, the PCAOB has announced sanctions related to:

- Exam cheating,
- Modifying work papers,
- Noncooperation with investigations,
- Unlawfully obtaining and using confidential PCAOB information, and
- Failure to have sufficient quality control processes in place to guard against ethical violations.

Let me be clear: the PCAOB will not tolerate unethical behavior.

I have said before, and I will say again, the PCAOB means business when it comes to enforcement.

We intend to use every tool in our enforcement toolbox and impose significant sanctions, where appropriate, to ensure there are consequences for putting investors at risk and that bad actors are removed. This includes substantial monetary penalties and significant or permanent individual bars and firm registration revocations.

Those who break the rules – whether they are ethical rules or auditing rules – should know we won't be constrained by the types of cases the PCAOB has pursued in the past. We won't be limited to the level of penalties that have been seen before. And we will seek admissions of wrongdoing in appropriate cases – for example, where the conduct is intentional or egregious.

Don't just take my word for it. This year, we imposed the highest total penalties in PCAOB history.

At the PCAOB, we are taking Senator Sarbanes' warning to maintain high standards quite literally with the most ambitious standard-setting agenda in PCAOB history.

When the PCAOB was first getting off the ground after SOX, it adopted existing standards on what was intended to be an interim basis.

Twenty years later, far too many of those interim standards remain unchanged.

As this audience knows better than most – our capital markets don't stand still. They evolve and grow. Practices change. Technology advances – relentlessly – with an impact on financial reporting and auditing.

To keep investors protected, our standards must keep up.

So, less than a year into this Board's term, we are actively working to update more than 30 standards within 10 standard-setting projects.

Just before Thanksgiving, the Board issued a new quality control (QC) standard for public comment.

I called it a watershed moment for the PCAOB, because QC systems lay the very foundation for how firms approach audits.

It is important to emphasize that some requirements in our proposed QC standard would apply to all firms registered with the PCAOB, including those that currently do not audit public companies or SEC-registered brokers and dealers. So, I encourage all registered firms to read the proposal and provide your perspectives.

Stakeholder feedback is critical in ensuring we get it right.

The deadline for comments is February 1, 2023. You can find more information on our website.

QC is foundational, but it is just one project on our agenda.

Earlier this year, we finalized amendments that strengthen requirements that apply to audits involving multiple audit firms. These amendments will require audit firms to ensure that lead auditors sufficiently plan, supervise, and evaluate the work of other auditors. The amendments take effect for audits of financial statements for fiscal years ending on or after December 15, 2024.

We are also on track to issue a proposal on the confirmation process before the end of this year. As you know, the confirmation standard addresses a process that touches nearly every audit. As we think about heightened risks for fraud in today's economy, confirmation can be a powerful tool for auditors to address such risks.

After confirmation, we are on track to issue several more proposals in 2023, updating our requirements in key areas that include:

- Illegal acts by clients,
- Going concern,
- The PCAOB's attestation standards, and
- Topics addressed by our AS 1000 series standards, such as due professional care.

We also have four projects on our mid-term standard-setting agenda. That means the staff is hard at work to advance standard setting for these projects, even if a Board action isn't expected in the next 12 months.

In addition to everything I've just mentioned, we also have a separate research agenda. Our research projects focus on whether there is a need for changes to our standards or some other regulatory responses.

We recently added a research project on firm and engagement performance metrics. This research project includes considering metrics already disclosed by firms along with work the PCAOB has done over the years.

You may recall that the PCAOB issued a concept release on firm and engagement performance metrics in 2015. We plan to leverage what we learned from this concept release as we evaluate the current environment related to this topic. Placing this project on our research agenda is a signal this Board is actively working to move it. We plan to move it to the standard-setting agenda in 2023 and advance it in short order from there.

Thanks to the hard work of our dedicated staff, the PCAOB has accomplished a great deal over the last year. And we have more work ahead.

As Senator Sarbanes said, "Trying to maintain high standards is a difficult job."

At the PCAOB it's our job. And we are driven by our mission: to protect investors.

Whether it's workers saving for retirement, parents saving to put their kids through college, or anyone who depends on the soundness of our capital markets to invest and build their own version of the American dream – quality audits protect people.

When I challenge you to uphold the highest standards in audit quality, it is with their families, their savings, and their futures in mind.

I urge you to keep them in mind as well. Resist complacency, sharpen your focus and meet your responsibility to verify the honesty our system depends on with a vigilance that is worthy of their trust.

I am excited to welcome my fellow Board Members on stage to continue the conversation with Julie.

About the PCAOB

The PCAOB is a nonprofit corporation established by Congress to oversee the audits of public companies in order to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports. The PCAOB also oversees the audits of brokers and dealers, including compliance reports filed pursuant to federal securities laws.

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