

SPOTLIGHT

Staff Priorities for 2024 Inspections and Interactions With Audit Committees

December 2023

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OVERVIEW

Inspecting is one of the most important tools the PCAOB has to protect investors in public companies and customers of brokers and dealers (“broker-dealers”). Inspections also provide an opportunity to inform the PCAOB’s standard-setting activities. This Spotlight aims to provide an overview of inspection priorities for 2024 of the Division of Registration and Inspections. Reminders and effective practices have also been included for registered public accounting firms (“audit firms” or “firms”), that were informed by recent inspection activity. This Spotlight is not intended to summarize the entirety of our planned inspection activities which, by design, include certain unpredictable procedures and selections and are adjusted, as necessary, for emerging topics.

Audit firms, public companies (“issuers”), broker-dealers, investors, audit committees and equivalents, and other stakeholders can expect that we will continue to focus our efforts in 2024 on improving audit quality in order to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports.

The 2024 inspection plan primarily covers the review of 2023 fiscal year-end audits, most of which will be completed by audit firms in the first quarter of 2024. Our inspection program is designed to review portions of selected audits of public companies and broker-dealers and to evaluate elements of an audit firm’s quality control (QC) system to assess the audit firm’s compliance with our standards and rules, as well as other regulatory and professional requirements that are applicable to the audit firm.

Our 2024 inspection program will consider overall business risks present in the audits inspected. A few of these business risks include:

- Persistent high interest rates, tightening of credit availability, and/or inflationary challenges.
- Disruptions in the supply chain and rising costs.
- Business models that are significantly impacted by rapidly changing technology.
- Geopolitical conflicts.
- Financial statements that include areas with a higher inherent risk of fraud, estimates involving complex models or processes, and/or presentation and disclosures that may be impacted by complexities in the public company’s activities.

KEY FEATURES OF OUR 2024 INSPECTION PROGRAM

Inspection Enhancements in 2024

Consistent with Goal 2 in the Board’s [Strategic Plan 2022-2026](#), we will take steps to enhance the PCAOB’s inspection program in 2024. We are also continually improving our inspection program, using a data-driven and risk-based approach, with a focus on riskier engagements and audit areas as described further in the section “Selections and Prioritized Sectors/ Industries.” Some of our enhancements include:

Increasing the number of engagements reviewed – Each year, several factors influence the number of public company and broker-dealer audits that we select for inspection.

These include prior inspection results and the emerging risks pertaining to a particular audit firm or industry. During 2024, in our efforts to enhance investor protection, we plan to increase the number of engagements we select for review at our annually inspected firms in response to heightened risks in certain industry sectors.

Expanding inspection procedures – During 2023 we began, and in 2024 we will continue, to perform inspection procedures on every engagement selected to assess compliance with certain aspects of the auditing standards related to independence, fraud, audit findings, audit committee communications, Form AP reports, the auditor’s report, engagement quality review, and audit documentation. These additional procedures enhance the robustness of inspections that assess audit firms’ compliance with applicable laws, rules, and standards.

Increasing focus on a firm’s culture of integrity and audit quality – Audit firms continue to face challenges delivering quality audits as evidenced by (1) the increasing trend of audit deficiencies in recent years and (2) deficiencies identified that have recurred for numerous years. We are interested in why these deficiency trends are not improving and whether audit firms’ cultures are playing a role in this failure to improve. See the section “Review of Culture at Firms.”

Performing quality inspections – Since 2019, the PCAOB has operated the Inspections Quality Group, an internal program aimed at applying best practices across inspection activities. In 2024, this group will continue to drive excellence across our inspection function by assessing the quality, consistency, and efficacy of our inspections.

Improving the timeliness of inspection reports – Considering the recommendation of the PCAOB’s Investor Advisory Group, we are taking additional steps to streamline our internal processes to enable timelier issuance of inspection reports. We are renewing our focus in this area and are committed to delivering meaningful results.

The Importance of Firm Quality Control Remediation

In February 2023 we published a Spotlight – “**Additional Insights on the Remediation Process**” – that reflects the staff’s current remediation program.

Selections and Prioritized Sectors/Industries

In 2024, in addition to continuing to select some engagements for review based on risk and some randomly, we will do the following:

- Continue our emphasis on selecting audits of companies engaging in merger and acquisition activities or business combinations.
- Continue our emphasis on selecting audits of broker-dealers that file compliance reports and others that provide customers with various investment opportunities, such as introducing brokers.
- Continue to select non-traditional audit areas to inspect.

Reminder – Other Required Filings

During the course of our inspection procedures, we may become aware of information or events that should have been reported, such as in a **Form 3** or **Form 4**.

Please carefully consider your filing requirements and available guidance. For example, the PCAOB issued **guidance on Form AP** in November 2023 that many audit firms might find helpful.

Beyond the selection factors mentioned above, we will place continuing emphasis on selecting audits of public companies in industries and sectors with specialized accounting and/or that may be negatively impacted by uncertainties and volatility in the economic and geopolitical environment. In 2024, our selection process will prioritize the following three sectors in particular:

- **Financials:** Regional banks experienced significant disruption in 2023 due to certain high-profile bank failures. The failure of an auditor to properly understand the business and management’s strategy degrades the ability to appropriately and diligently exercise professional skepticism and professional judgment. Areas requiring particular auditor attention include, but are not limited to:
 - o Ongoing changes in interest rates, which can have a material effect on a company’s liquidity position.
 - o Allowance for loan and lease losses.
 - o Classification of investments as available-for-sale or held-to-maturity.

- o Valuation of investments in hard-to-value securities.
- o Ability to meet margin requirements.
- o Ability to meet long-term debt obligations.
- o An entity’s ability to continue as a going concern.

Our risk selection factors will be calibrated to intentionally select more audits of regional bank public companies and mutual funds with Level 3 investments, or other specific audit challenges.

- **Information Technology:** Public companies in this sector, which include technology, hardware, and the semiconductor industry, have financial statement accounts, disclosures, and related internal controls that tend to be complex due to revenue recognition, other significant judgments, and contractual arrangements with customers. The risk of fraud due to management override, although not unique to this sector, is often heightened given earnings pressures. Disruptions to the supply chain can also impact revenue recognition. Our selection process will continue to scrutinize audits in this sector.
- **Other:** Continuing emphasis will be placed on selecting audits of public companies that apply industry-specific or sector-specific accounting. Selections may also consider audits of public companies that hold significant assets that may have declined in value, such as collateralized commercial real estate debt.

2024 INSPECTION CONSIDERATIONS

Our 2024 inspection plan focuses on risks and other considerations that – based on PCAOB standards and communications – should be important for auditors when planning and performing risk assessments and audit procedures. We discuss certain of these considerations below. Auditors may want to consider additional focus in these areas as they plan their audit procedures.

Broker-Dealers

Our inspection plan also includes procedures over broker-dealers. The “[Annual Report on the Interim Inspection Program Related to Audits of Brokers and Dealers](#)” was published in August 2023. The report provides additional information about our 2022 inspection approach for firms that audit broker-dealers. It also includes a summary of our 2022 inspection observations, a description of good practices, and recommended actions for firms. In 2024, we will continue to focus on the challenges and recurring deficiencies that we observed in

Effective Practice – Testing Controls With a Review Element

Auditors often select and test management review controls in audits of internal control. Such management reviews might be performed to monitor the results of operations, such as (1) monthly comparisons of actual results to forecasted revenues or budgeted expenses; (2) comparisons of other metrics, such as gross profit margins and expenses as a percentage of sales; and (3) quarterly balance sheet reviews. These reviews typically involve comparing recorded financial statement amounts to expected amounts and investigating significant differences from expectations.

As with other types of controls, the auditor should perform procedures to obtain evidence about how a management review control is designed and operates to prevent or detect misstatements, including identifying and resolving items for follow-up. Verifying that a management review control was signed off or “approved” provides little or no evidence by itself about the control’s effectiveness.

As an example, for a management review control, the threshold for investigating deviations or differences from expectations relative to materiality is an indication of a control’s precision. A control that investigates items that are near the threshold for financial statement materiality has less precision and a greater risk of failing to prevent or detect misstatements that could be material than a control with a lower threshold for investigation. Please see Staff Audit Practice Alert No. 11, ***Considerations for Audits of Internal Control Over Financial Reporting***, for additional information.

Auditors should exercise care in evaluating the potential misstatement resulting from a control deficiency. These potential misstatements have been called the “could factor.” When assessing review controls and the severity of control deficiencies the potential misstatement should be considered. The “could factor” evaluation includes assessing the total population of transactions or amounts exposed to the deficiency in the impacted accounts or classes of transactions.

those inspections and that we continue to see in the field.

Recurring Deficiencies

In our July 2023 Spotlight – “Staff Update and Preview of 2022 Inspection Observations” – we discussed recurring deficiencies that include deficiencies in audit work related to revenue and related accounts, accounts affected by business combinations, inventory, long-lived assets, including goodwill and intangible assets, and equity and equity-related transactions. Testing controls with a review element has also been a significant recurring deficiency. These deficiencies have remained relatively consistent over the periods, and significant estimates, evidence, and/or data and reports used to support audit conclusions are often a component of these violations. A component of our inspections will consider recurring deficiencies previously identified.

Evaluating Audit Evidence

Inherent to an audit – and an aspect of our inspection procedures – is the consideration of due professional care, which, among other things, requires the auditor to exercise professional skepticism. Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence. The auditor uses the knowledge, skill, and ability called for by the profession of public accounting to diligently perform, in good faith and with integrity, the gathering and objective evaluation of evidence. Gathering and objectively evaluating audit evidence requires the auditor to consider the sufficiency and appropriateness of the evidence. Since evidence is gathered and evaluated throughout the audit, professional skepticism should be exercised throughout the audit process.

Understanding the Company and Its Environment

Understanding the company and its environment is an important initial step to planning the audit. The auditor should obtain an understanding of the public company and its environment to understand the events, conditions, and activities that might reasonably be expected to have a significant effect on the risks of material misstatement. We plan to continue assessing how the auditor’s understanding of the public company and the auditor’s evaluation of significant changes in the public company from prior periods, including changes in the public company’s internal control over financial reporting, affect the risks of material misstatement.

Use of Other Auditors

Results from our inspections continue to have a significant level of findings, which further increases the importance of the principal auditor (under the revised standard, lead auditor) to properly plan and oversee the work of other auditors. We plan to continue to perform procedures related to the use of the work of other auditors on all reviews where there was significant involvement of other auditors. It is the principal auditor’s responsibility to confirm that the other auditor who plays a substantial role is registered with the PCAOB.

Going Concern

Under U.S. and international financial reporting frameworks, the continuation of a company as a going concern is presumed as the basis for preparing financial statements unless and until the company no longer reports under this basis, such as by changing to the liquidation basis of accounting. Preparation of financial statements under this presumption

is commonly referred to as the going concern basis of accounting. The auditor is required to evaluate a company's ability to continue as a going concern under both federal securities law and PCAOB auditing standards. We continue to select public company audits where these challenges are potentially present to review the evaluation made by the auditor.

Critical Audit Matters

Our 2022 [interim analysis report](#) on critical audit matters (CAMs) indicated that the average number of CAMs per audit report has declined over time, and the proportion of audit reports that communicate just a single CAM has increased. We have also noted continuing high levels of deficiencies, both at the disclosure and/or evaluation levels. We plan to continue our focus on audit firms' compliance with the requirements for CAMs for all public company audits selected for review, where CAMs are applicable.

Reminder – Critical Audit Matters

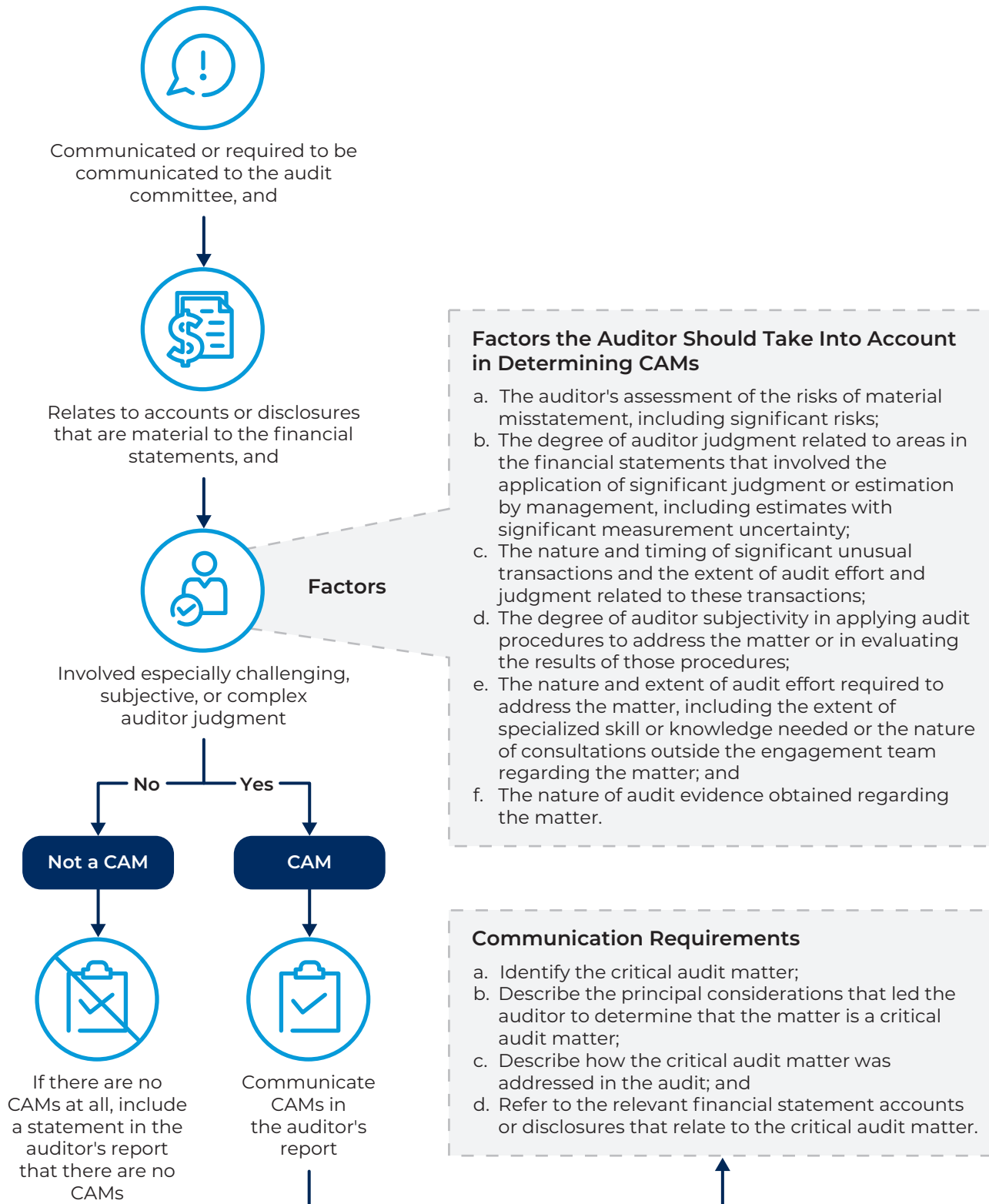
Many audit firms have created practice aids and templates to provide guidance to engagement teams determining and communicating critical audit matters. These practice aids are only helpful if completed appropriately. The following illustration was included in our adoption of the standard, and many firms may find it helpful as a reminder of the high-level requirements. We have highlighted the factors that should be taken into account when considering especially challenging, subjective, or complex auditor judgments.

Implementation Resources for PCAOB Standards and Rules

The PCAOB supports the implementation of our standards and rules to improve the quality of audit services. Visit our [Implementation Resources for PCAOB Standards and Rules](#) website page to learn more about the standard-setting process, sign up for project updates, and find materials that may support the implementation of select standards and rules, including the following:

- **Auditing Accounting Estimates, Including Fair Value Measurements**
- **Auditor Reporting**
- **Auditor's Use of the Work of Specialists**
- **Confirmation**
- **Form AP**
- **Supervision of Other Auditors**

Determining and Communicating Critical Audit Matters (CAMs)



TECHNOLOGY-RELATED CONSIDERATIONS

New technologies often require new skills and considerations. One of the potential challenges for new technologies is ensuring that auditors have the appropriate knowledge and skills to efficiently and, perhaps more importantly, effectively incorporate or address these new technologies in their audit. Given the rapid pace of technological evolution in financial reporting and auditing, our inspectors will also focus on the following technology-related areas:

Digital Assets

Activities associated with digital assets may involve heightened risks to investors, public companies, and broker-dealers. These risks include volatility of digital assets values, lack of transparency related to ownership and purpose, and fraud. Digital assets require (1) an appropriate risk assessment, (2) understanding of the control environment, including information technology controls, (3) an understanding of the controls over the existence and ownership of the digital assets, including ongoing safeguarding of private keys, and (4) an appropriately planned audit response.

We will continue to focus on identifying public companies and broker-dealers that have material digital asset holdings and significant transactions related to digital assets, and we will prioritize selecting those engagements for review, where appropriate. Please see our June 2023 Spotlight, "[Inspection Observations Related to Public Company Audits Involving Crypto Assets](#)."

Cybersecurity

The risk of cybersecurity attacks to public companies and broker-dealers is always present and increases for those public companies and broker-dealers who have not understood their vulnerabilities and are

unprepared to identify and react to cyber incidents when they do occur.

For audits selected for review, we will request that the firm discuss how cybersecurity risk is considered and incorporated, if applicable, into the planned audit response. For audits selected for review where a cyber incident has been identified, we will review how the firm evaluated the public company's response, including how the firm may have modified its planned audit response. We will also review the [incident disclosure](#) made in compliance with the U.S. Securities and Exchange Commission rules requiring, among other things, public companies to disclose material cybersecurity incidents they experience and the audit firm's related audit response, if appropriate.

Use of Data and Technology

Business and financial reporting processes are changing as technology rapidly evolves. For example, companies are expanding (1) their use of cloud services to process and store financial reporting data, (2) their revenue channels by adding e-commerce platforms for online transactions, or (3) their use of artificial intelligence to initiate customer content or process financial transactions. These changes affect the nature, timing, preparation, and use of financial information prepared by the public company and increase the complexity of the public company's information technology systems and related controls. Auditing information technology general and application controls has been a recurring area of audit deficiencies.

In addition, auditors of both public companies and broker-dealers are expanding their use of technology-based tools, including technology-assisted analysis of information in electronic form, to plan and perform audits. The increased use of these technology-based tools could affect areas such as (1) the auditor's risk assessment and response to identified risks of material misstatement whether due to error or

fraud, (2) the nature and extent of information available to auditors and preparers, and (3) the audit firms' QC systems.

We will continue to inquire about changes in the use of technology in financial reporting and auditing. For audits selected for review, we will evaluate the use of technology related to audit procedures, particularly focusing on instances where technology is used in procedures to respond to identified risks of material misstatement.

TARGET TEAM

The target team performs engagement reviews and other firm process reviews that are focused on emerging risks and areas of specific focus across programs and firms. In December 2023, we plan to publish a Spotlight – “Observations From the Target Team’s 2022 Inspections” – that discusses our look across audit firms related to initial public offerings, including mergers of a public special purpose acquisition company with a non-public operating company, climate-related matters that can materially impact a company’s financial statements, and the use of audit firms’ shared service centers. In 2024, our target team plans to continue looking across firms and programs for insights on timely topics or emerging risks.

REVIEW OF CULTURE AT FIRMS

To consistently execute quality audits, a firm’s senior leadership needs to promote and embrace a culture of integrity and audit quality (sometimes referred to by audit firms as “tone at the top” or firm culture). Therefore, as described above, as an enhancement to our inspection program, we have created a small team to initially evaluate culture across the “U.S. Global Network Firms” category of firms inspected by the PCAOB. This initiative includes interviewing firm personnel and

evaluating other documentation, as deemed necessary, as part of our QC procedures. We will use this information to inform our understanding of audit firms’ cultures and the impact on audit quality. Aggregated results will be included in a future publication.

INTERACTIONS WITH AUDIT COMMITTEES

Audit committees are vitally important to our capital markets—both to the public companies seeking capital and to the investors who provide that capital. And, for a number of reasons, the PCAOB and audit committees have a special relationship that contributes to the integrity of the capital markets. We have a shared purpose: protecting investors and maintaining the integrity of our capital markets.

Audit Committee Outreach

Dialogues with audit committee chairs continue to provide valuable insights, refer to our September 2023 Spotlight, “[2022 Conversations With Audit Committee Chairs](#).” We plan to continue to invite the audit committee chairs on public company audits selected for review on U.S. annually inspected firms to these dialogues and to perform similar procedures on a sample of our smaller U.S. triennial audit firms during 2024. Please see our June 2023 Spotlight, “[Audit Committee Resource](#).”

Questions for Audit Committees to Consider

In the context of the PCAOB’s 2024 inspections, these suggested questions may be of interest to audit committee members to consider amongst themselves or in discussions with their independent auditors. These questions supplement and build on other sets of questions we have suggested in recent Spotlights such as “[Staff Update and Preview of 2022 Inspection Observations](#)” (July 2023) and “[Audit Committee Resource](#).”

These questions, designed principally to further two-way communication, represent the views of PCAOB staff and not necessarily those of the Board. The PCAOB does not set standards for, or provide authoritative guidance on, audit committee conduct.

1. How does the audit firm ensure that audit engagement team members have the appropriate understanding of our business so they can effectively perform their assignments?
2. Every year the auditor asks this audit committee if it has knowledge of fraud, alleged fraud, or suspected fraud affecting the company. What else has the auditor considered when planning and performing the audit to obtain reasonable assurance about whether the company's financial statements are free of material misstatement due to error or fraud?
 - a. Did the auditor consider confirming significant revenue transactions with the counterparty to test for side arrangements?
 - b. If the company has digital assets, consider asking the auditor how existence and ownership of the digital assets, including ongoing safeguarding of private keys, were tested.
3. How would you, the auditor, commit fraud in our organization, and if you were an employee or member of management, what would you do to prevent it?
4. If the auditor has identified information, events, or conditions that suggest that the public company's ability to continue as a going concern is in doubt, consider asking:
 - a. Did the auditor conclude that substantial doubt exists or would exist absent management's plan?
 - b. When the auditor assessed management's plans to mitigate the effect of the substantial doubt, did the auditor find the plans aggressive?
- c. Is the likelihood that such plans can be effectively implemented realistic based on the current situation?
- d. Does the auditor find management's disclosure regarding the substantial doubt adequate?
5. If other auditors are used, consider asking:
 - a. How did the auditor ensure that the other auditors are independent?
 - b. Did the auditor review the work of the other auditors, and, if so, was it performed appropriately and to the auditor's satisfaction?
6. If portions of the audit were outsourced to a shared service center, how did the auditor determine that service center personnel executed the procedures appropriately?
7. What challenging, subjective, or complex auditor judgment did the auditor apply during the audit? Did the auditor's application of challenging, subjective, or complex auditor judgment result in disclosure of a CAM? Why or why not?
8. If a cybersecurity event occurred, consider asking how the audit response was impacted. Also ask about the auditor's impression of the company's governance to protect systems, information, and other assets.
9. What is the auditor's overall impression of the company's use of technology?
 - a. Did the auditor observe any areas during their testing that warrant audit committee attention?
 - b. Was the auditor able to effectively use technology in audit procedures, or was the company unable to provide appropriate/sufficient data to be able to utilize technology effectively?

10. What is the audit firm's use of technology? What was applied during the audit?
11. What is the auditor's candid impression of the audit committee's oversight of the internal audit function and how the internal audit plan addresses the company's significant risks?

TELL US WHAT YOU THINK

Was this Spotlight helpful to you? In fulfilling our mission to serve investors and the public, the PCAOB wants to know how we can improve our communication and provide information that is timely, relevant, and accessible. We welcome comments on this publication or other matters. You can fill out our [short reader survey](#) or email us at info@pcaobus.org.

Effective Practice – Audit Committee Communications

AS 1301.10d, from ***Communications with Audit Committees***, requires the engagement team to disclose the names, locations, and planned responsibilities of other independent public accounting firms or other persons, who are not employed by the auditor, that perform audit procedures in the current period audit.

We have issued frequent inspection findings related to audit committee presentations regarding the planned engagement team that failed to provide sufficient or complete information as required under the standard.

An effective practice for firms can include referencing a separate attachment to the presentation that includes a table with the legal firm name(s) or other person(s) who are not employed by the lead auditor, their location, and their planned responsibilities. Planned responsibilities may include:

- A component audit team to which work has been referred.
- Staff augmentation to the lead auditor team or a component audit team.
- An affiliated firm with specialized skill or knowledge utilized by the lead auditor team or a component team.
- Involvement of a shared service center.

Firms with multiple legal entities should consider all planned participation.

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