SFTF

SMALLER FIRM TASK FORCE

January 8, 2025
By email: rule-comments@sec.gov

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: SECURITIES AND EXCHANGE COMMISSION [Release No. 34-101724; File No. PCAOB-2024-06] Public Company Accounting Oversight Board; Notice of Filing of Proposed Rules on Firm and Engagement Metrics and [Release No. 34-101723; File No. PCAOB 2024-07] Public Company Accounting Oversight Board; Notice of Filing of Proposed Rules on Firm Reporting.

Dear Office of the Secretary:

The Center for Audit Quality (CAQ) Smaller Firm Task Force (SFTF) provides a forum for smaller and medium-sized CAQ member firms (consisting of non-affiliate firms (NAFs)[1] including a mix of triennially inspected firms that generally audit mid to smaller market cap issuers) to discuss technical and regulatory issues that impact their public company auditing practices. It also facilitates meetings with stakeholders, including PCAOB staff and Board members, to offer the perspective of smaller firms on practice and regulatory matters. The SFTF provides resources and support to smaller and medium-sized firms, making sure they are well-represented and their concerns are addressed in the broader professional community.

This comment letter represents the views of the SFTF regarding the totality of the PCAOB's standard setting activities, including their recently adopted *Firm and Engagement Metrics* and *Firm Reporting* rules (rules or new requirements).

The SFTF agrees with the following overall concerns raised in the CAQ comment letters submitted to the SEC on *December 26, 2024* and January 2, 2025:

- The Securities Exchange Act of 1934 (Exchange Act) requires that whenever the SEC is engaged in rulemaking, or in the review of a rule of a self-regulatory organization, and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will *promote efficiency, competition, and capital formation* [emphasis added].[2] Combining this

[1] The CAQ is a nonpartisan public policy organization serving as the voice of US public company auditors and matters related to the audits of public companies. The CAQ promotes high-quality performance by US public company auditors; convenes capital market stakeholders to advance the discussion of critical issues affecting audit quality, US public company reporting, and investor trust in the capital markets; and using independent research and analyses, champions policies and standards that bolster and support the effectiveness and responsiveness of US public company auditors and audits to dynamic market conditions. This letter represents the observations of the CAQ based upon feedback and discussions with certain of our member firms, but not necessarily the views of any specific firm, individual, or CAQ Governing Board member.

[2] 15 U.S.C. § 78c(f).

requirement with Section 107(b)(3) of SOX,[3] Section 78c(f) of the Exchange Act requires the SEC to conduct its own assessment to determine the effects of a PCAOB proposal on *efficiency, competition, and capital formation*, which requires an economic analysis. The Board has not sufficiently analyzed the impact of the final rules on efficiency, competition, and capital formation.

- The PCAOB has failed to conduct an adequate cost-benefit analysis of the required disclosures.

- The PCAOB has not demonstrated the desirability or decision-usefulness of the required disclosure by stakeholders.

- The PCAOB has not gathered and considered public input to adequately inform and develop final rules that meet the needs of stakeholders and minimizes the risk of unintended consequences.

- The PCAOB's rush to adopt its final rules and submit them to the Commission for approval,[4] has not allowed ample time for the Board and its staff to sufficiently address the many serious comments and concerns communicated in the comment letter process.

- Some of the reporting requirements the PCAOB seeks to impose represent an overreach of the PCAOB's jurisdictional authority as they have little relationship with the PCAOB's enumerated powers under the Sarbanes-Oxley Act of 2002.

We appreciate the efforts made by the PCAOB staff to meet with the CAQ staff and our Task Force in particular to discuss comments and concerns on the Firm Reporting proposal as they relate to smaller firms.[5] A main recommendation made in this meeting was for the PCAOB to better demonstrate what they were trying to achieve with certain of the firm reporting requirements and whether the disproportionate costs to smaller firms of aggregating and reporting such information (including onramp costs to develop systems to capture the required data) outweighed the benefits. We do not see this recommendation incorporated into the final rules. The Board's rush to finalize the rules in record time has not provided the staff with ample opportunity to adequately consider and respond to this and other overarching concerns raised by the public in the comment letter process.

We also wish to emphasize to the Commission the significant concerns raised by the SFTF in our comment letter[6] to the PCAOB on June 20, 2024 regarding the unprecedented pace, volume and timing of recent PCAOB's standard-setting activities and the resultant crippling impact on smaller firms, smaller companies and our capital markets. The following overarching concerns are among those included in the letter that still remain:

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[3] 15 U.S.C. § 107(b)(3) states that the SEC shall approve a PCAOB proposal "if it finds that the rule is consistent with the requirements of this Act and securities laws, or is necessary or appropriate in the public interest or for the protection of investors."
[4] With an eye toward the calendar, specifically the impending presidential inauguration date of January 20, 2025.
[5] This meeting was held less than two weeks before the PCAOB's Open Meeting to vote on the final rule. The timing of the Open Meeting made it clear that the PCAOB staff were not allotted sufficient time to incorporate our input.
[6] It should be noted that, in the over 15-year existence of the CAQ, the SFTF had not separately commented on PCAOB standard setting or other PCAOB activities.

1. **Importance of smaller businesses to the overall capital markets.** Small public companies are vital to the economic backbone of our communities and overall economy.[7] Our country needs smaller businesses, and smaller businesses need affordable capital. The implementation of the Sarbanes-Oxley Act of 2002 (SOX) significantly increased audit fees and the regulatory cost of accessing the public market, disproportionately impacting the ability of smaller companies to access the capital markets. The ever-rising cost of regulation has resulted in small companies either going private or being deterred from entering the capital markets.[8]

2. **Importance of smaller accounting firms to smaller companies.** Smaller accounting firms play a vital role in providing quality audits to emerging, small and middle-market companies, all of whom require access to the capital markets to grow their businesses. Smaller accounting firms are deeply rooted in the local communities they serve, both in terms of auditing smaller companies as well as providing employment opportunities and career advancement for a diverse workforce. Ultimately, these accounting firms play a critical role in assuring the quality of information investors rely on to have confidence and promote effective functioning capital markets.

3. **More pronounced/disproportional impact of PCAOB regulation overload on smaller firms and companies.** Concerns expressed by smaller firms regarding the disproportional impact of increasing regulatory burdens on smaller firms are real. Because their public company audit practices are smaller than the larger firms, the costs incurred to implement administrative data collection processes to comply with the proposed reporting requirements are spread across a smaller number of audit clients who can't absorb significant increases in audit fees. In other words, it is difficult for smaller firms to pass on regulatory costs to their clients, often forcing them to leave the public company auditing arena,[9] resulting in increased market concentration, which in turn forces smaller companies to engage larger more expensive (and often non-local) firms to perform their audits. We observe that Board stated, "Our oversight activities indicate that noncompliance with auditing standards is higher among smaller firms [footnote excluded]. Therefore, to the extent smaller firms tend to exit rather than larger firms, as commenters contended, then audit quality could improve on average as issuers switch to larger firms."[10] We disagree with this notion. There are plenty of smaller firms that have high rates of compliance, and if the rules drive these firms out of the market, audit quality would not be improved. As discussed above, driving smaller (often local) firms out of the market makes it more costly and thus more difficult (if not impossible) for many smaller companies to comply with auditing requirements and access the capital markets. Moreover, the Board has not adequately studied the impact of smaller firms deciding to leave the public company audit market as a result of the final rules.

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[7] 99.9% of all businesses are small businesses, 43.5% of the U.S. GDP is created by small businesses, and 63% of net new jobs are created by small businesses (see See https://www.sec.gov/files/2023-oasb-annual-report.pdf.)
[8] In 2022, the number of exchange-listed IPOs dropped to its lowest point since 2009. (See https://www.sec.gov/files/2023-oasb-annual-report.pdf.)
[9] According to a recent survey conducted by the American Institute of CPAs, nearly 75% of respondents would consider eliminating their public company audit practices if the Firm Reporting and the Firm and Engagement Metrics Proposals are adopted.
[10] See Adopting Release 2024-012, page 243.

4. **Impact on ability of smaller firms to attract and retain talent.** Commenters have previously shared with the PCAOB the well-documented staffing shortages and pipeline issues in the accounting profession. With fewer professionals entering the space coupled with increasing complexity at companies and a robust regulatory environment, auditors in firms of all sizes are stretched thin and the impact on smaller and medium-sized firms is even more pronounced. Attracting qualified and competent personnel overall is a challenge but attracting and keeping talent to perform PCAOB engagements is compounded given the additional costs – whether reputational, time or wellbeing – associated with the work. Adding to the resource constraints is the need for additional personnel that would be required to collect, analyze, review and report the reams of data required by the rule, the utility of which is uncertain. Smaller firms fully understand their public interest and gatekeeper role in the capital markets but their personnel are beginning to express the desire to exit this work due to the increasingly burdensome regulatory environment.

These concerns are significant and they remain unresolved. As such, we urge the Commission to act in the public interest by declining to approve the final rules until 1) sufficient research and economic analysis can be conducted and 2) public feedback can be carefully considered, including feedback relating to the impact of these requirements on smaller firms, smaller companies and the communities in which they exist.

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The SFTF appreciates the opportunity to comment on the final rules, we look forward to future engagement and we encourage the Commission and PCAOB Board to proactively seek out engagement with auditors, audit committee members and investors on these topics. As the Commission continues to gather feedback from other interested parties, we would be pleased to facilitate a meeting of the Smaller Firm Task Force with the Commission and/or its staff regarding the views expressed in this letter. Please address meeting requests to Annette Schumacher (aschumacher@thecaq.org).

Sincerely,

Members of the Smaller Firm Task Force

cc:

SEC
Honorable Gary Gensler, Chair
Caroline A. Crenshaw, Commissioner
Jaime Lizárraga, Commissioner
Hester M. Peirce, Commissioner
Mark T. Uyeda, Commissioner
Paul Munter, Chief Accountant