The Public Company Accounting Oversight Board

Name

Course

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Date

The role of PCAOB in improving reliability of audited financial statements

The Public Company Accounting Oversight Board (PCAOB) is a non-profit private corporation formed under the Sarbanes-Oxley Act (SOX-2002) to conduct supervisory roles to all accountants or auditors involved in producing audit reports for public companies (Palmiter, 2008). The board's core mandate is to ensure that the independent auditors observe due procedures while auditing public companies. In addition to this, the body registers, conducts investigations and issues disciplinary measures to public accounting firms found guilty of auditing malpractices (Palmiter, 2008). The board also ensures that public accounting firms observe the SOX Act to the latter. The establishment of PCAOB has greatly enhanced reliability of audited financial statements for the public users of information. The following section provides a detailed analysis of the important role played by PCAOB.

PCAOB routinely conducts inspections upon public accounting firms to ensure that they adhere to all the accounting standards. A section of the reports dubbed 'part 1' is made available to the general public. In circumstances where material concerns are identified, the board prepares another report dubbed 'part 11', which is kept private as further investigations are conducted. Part 11 of the report is only made public when the board finds material weaknesses in the accounting firm's quality control systems, usually after one year of investigation (PCAOB, 2008). In such a case, the board may issue disciplinary action such as sanctions upon the affiliated accounting firm. Such investigations and disciplinary action taken against public accounting firms help in ensuring that public accounting firms adhere to the expected professional standards while conducting audits. This increases confidence upon users of audited reports.

Since its inception, PCAOB has brought to book several audit firms and individuals found to have violated standards while carrying out their auditing duties. For instance in 2014, the board instituted disciplinary action against two auditing firms found to have violated auditing standards. In addition, four individuals involved in the scam were also investigated and disciplinary action taken against them. The firms, Jeffrey & Company and Berman W. Martinez Y Asociados, had their licenses revoked after they failed to observe auditing standards (‘PCAOB,’ 2014b). Such companies can no longer audit public company accounts, a similar fate to the individuals concerned. Such disciplinary action taken against public accounting firms have ensured that they exercise diligence while carrying out their auditing duties. PCAOB has thus been effective in improving the reliability of public audited accounts among users of the information.

Prior to the establishment of the Board in 2002, public accounting firms were self-regulated. During this period, the number of scandals rocking public companies was increasing at an alarming rate. For example, Enron and WorldCom scandal in 2002 which drew a lot of public anger and attention. Following the massive scandals, there was a great need to establish an independent body that would amend the failures of the previous body. PCAOB was created to act as an independent watchdog over public accounting firms. In self-regulation, the major concern is that the regulating body may often fail to sanction public accounting firms found to have committed fraud or failed to have observe standards due to fear of a bad public image plaguing the whole industry. The establishment of PCAOB arrayed such fears and helped restore public confidence in public companies' audited financial reports.

PCAOB often conducts oversight activities which are aimed at identifying weaknesses in internal control systems and risks that may be involved. The board then issues detailed reports of the findings to the public. Such reports are useful to the public and also put pressure on public accounting firms to comply with standards and protocols while carrying out their duties. PCAOB routinely revises auditing standards where necessary usually following suggestions from investors, public accounting firms or other relevant authorities. This has helped seal any loopholes that negatively affected audit practice. The continued effort to revise auditing standards has further restored confidence among investors as well as the general public. For instance in 2013, the board amended reporting standards used by auditors to include more details ('PCAOB,' 2014a). Prior to the amendment, auditors were only required to report a pass or fail concerning the accuracy of financial statements. Following the new standard, auditors must go a step further and explain why they made such a decision.

By December 2011, PCAOB had already taken action against more than 45 public accounting firms. Of the 45 issues, 41 had already been settled (Hardison and Pashkoff, 2012). The board's success in unearthing public accounting firms non-conformance issues can only be attributed to the immense authority it has over all firms registered under it. In addition, PCAOB has a more definite or narrower role unlike the Securities and Exchange Commission (SEC). PCAOB is tasked with investigating audit failures by firms, lack of proper adherence to auditing standards, and situations where auditing firms do not comply when being investigated. SEC has a wider role in that it is also tasked with investigating public firms and their employees of any misconduct (Hardison and Pashkoff, 2012). The narrow roles assigned to PCAOB have made the board more efficient in carrying out its duties. This provides more assurance to public users of accounting information on reliability of audited financial reports (Hardison and Pashkoff, 2012).

Question 2

Impact of PCAOB to the accounting profession following a shift from self to federal regulation

The impacts of the shift from self regulation to federal regulation are both pervasive and profound to the accounting profession. As mentioned earlier, PCAOB was formed as a result of massive failures by the then commission, American Institute of Certified Public Accountants (AICPA), to enforce security laws and standards during public firm audits. The ever increasing cases of massive scandals, such as Enron Scandal had eroded so much confidence upon the users of public information that it was deemed necessary for an independent board to be set up to restore the lost confidence.

Federal regulation meant that all accounting firms had to register under a common body. Since the establishment of the board, all public accounting firms were required to register and have their capability to assess public firms determined by the board (Quick, Turley & Willekens, 2007). All public firms had to meet the set criteria in order to be registered by the board. Any accounting firm that failed to register was barred from auditing public firms until all requirements were fulfilled. Deregistration is usually carried out by SEC. The board also outlined a series of standards or laws that all registered accounting firms were expected to follow (Quick, Turley & Willekens, 2007).

The shift to federal established discipline in a profession that had been tainted by massive scandals following most auditors' disregard of set standards and rules while carrying out audit of public firms. The board is mandated with ensuring discipline and investigating public accounting firms suspected of disregarding set standards and rules (Quick, Turley & Willekens, 2007). As such, any accounting firms or professionals that fail to observe expected procedures face certain penalties which the board determines. These penalties include censoring, fines, deregistration, revocation of licenses among others. Such measures ensure that auditing firms and professionals observe due protocols to avoid negative consequences from the board.

The establishment of PCAOB has greatly improved the quality of audits by accounting professionals. Since the enactments of the SOX Act, accounting firms are keen on the quality of staff they hire (Pritchard and Puri, 2006). This is because they are aware of the sanctions they may face when their employee conduct low quality work. When accounting firms register with PCAOB and other regulatory bodies, they commit themselves to observe the required standards and follow all rules. Auditors often receive advice on how to improve quality of their audit work from the board. The major weakness in self-regulation lay in the fact that the regulating bodies would fail to sanction public accounting firms for fear of a bad public image on the whole profession (Pritchard and Puri, 2006).

PCAOB have also had a positive impact on accounting professionals in terms of sharing important information in terms of new procedures and standards that improve the audit process. The board routinely holds meetings with auditors and relevant bodies to brief them on new standards and procedures that basically keep them abreast with new developments in the industry. The board often conducts training sessions to sharpen auditors' skills in inspection findings and other audit procedures ('PCAOB,' 2014a). In addition, the board often discusses weaknesses discovered in audit control systems and seeks ways of remediating those weaknesses. Such forums have greatly helped auditors improve the quality of their audit work and improve reliability of audit reports among users ('PCAOB,' 2014a).

PCAOB is recognized for establishing independence in the accounting profession. Over the years, the board has been relentless in seeking the best ways to increase auditors' independence. Among the proposals by the board is mandatory rotation by audit firms in a bid to reduce development of client-auditor relationship ('PCAOB,' 2014b). The board also came up with ways to improve the relationship between auditors and audit committees. The relationship between the auditors and the audit committee is important since it also determines the objectivity of the audit. The audit committee is charged with the responsibility of overseeing how the audit is conducted. Improving communication between the audit committee and the auditors has thus helped improve the integrity of the audit reports.

In conclusion, the creation of PCAOB has been effective with improving the reliability of audited financial statement for the public users. The board is charged with the mandate to conduct inspections on all public accounting firms in order to ensure they adhere to security laws and all the established standards. The board also settles cases of noncompliance by taking disciplinary issues against audit firms and professionals who fail to follow standards and rules. PCAOB have positively impacted the accounting profession by improving the quality of audits through training and enforcement of standards and rules.

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