Quest Diagnostics

August 15, 2017

Brent J. Fields, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Proposed Rule on the Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion, and Departures from Unqualified Opinions and Other Reporting Circumstances, and Related Amendments to Auditing Standards

File Number PCAOB-2017-01

Dear Mr. Fields:

Quest Diagnostics Incorporated ("Quest") appreciates the opportunity to submit its views to the U.S. Securities and Exchange Commission (the "SEC" or "Commission") regarding the Public Company Accounting Oversight Board's (the "PCAOB") proposed new auditing standard designed to enhance the usefulness of the auditor's report entitled The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion (the "Proposed Standard"). Quest is the world's leading provider of diagnostic information services, which includes providing clinical testing services such as routine testing, non-routine (including advanced diagnostics) testing, and anatomic pathology services, as well as related services and insights. We provide interpretive consultation with one of the largest medical and scientific staffs in the industry.

We know that a number of companies and preparers have commented on the Proposed Standard to date, including those that are considered leaders in their respective industries and fields. Many commenters have raised broader concerns similar to the ones we outline in this letter. We echo the broader concerns regarding the Proposed Standard that have been raised throughout the PCAOB's process and do not believe that the PCAOB has adequately addressed them in the Proposed Standard. In this letter, we identify the issues with which we are most concerned.

While we support the PCAOB's objective to improve the relevance and usefulness of the auditor's report, including certain proposed enhancements to the report, our core concerns with the Proposed Standard relate to the requirement that auditors be required to disclose critical audit matters ("CAMs") in the auditor's report.

The Proposed Standard defines CAMs as any matter arising from the audit that was communicated or required to be communicated to the audit committee and that involves material audit specific information and involves especially challenging, subjective, or complex auditor judgment.

The addition of CAMs to an auditor's report departs significantly from the current financial reporting framework where the company is responsible for financial statement and related disclosures by altering the current distribution of duties so that the auditor shares responsibility for reporting. We are most concerned about the potential for the auditor to independently disclose information in their report about matters that the company may have already independently concluded does not need to be disclosed under the current financial reporting framework and SEC reporting requirements.

While we acknowledge that, in practice, it is likely that in many situations the auditor will collaborate with a company on substantive disclosures related to matters covered by CAMs to ensure there is consistency between the auditor's report and the company's disclosure, it is also likely that there will be instances where the auditor will make a conclusion to disclose information that the company has concluded is commercially sensitive, inappropriately timed or otherwise unnecessary to disclose. Such conflict is unavoidable because the Proposed Standard provides that the auditor has the authority to disclose such information if "such information is necessary to describe the principal considerations that led the auditor to determine that a matter is a critical audit matter or how the matter was addressed in the audit." Indeed, the PCAOB acknowledges as much and attempts to justify this conflict because "the PCAOB believes it is in the public interest for the auditor to include that information in the auditor's report." An error inherent in the conclusions drawn by the PCAOB in the Proposed Standard is that information drawn from the audit process is different from the information about the company contained in the financial statements. Management has responsibility for its financial statements, including an assessment of the challenging, subjective, and complex judgments faced when preparing its financial statements. CAMs could also undermine the role of the audit committee, which is independent from management and already represents the shareholders in its oversight of and direct communications with the auditor.

It is also an unfortunate reality that any discrepancies between the auditor's report and company disclosure related to matters covered by CAMs may lead to lawsuits from plaintiffs – most being meritless complaints that are settled to avoid litigation costs even when there is no wrongdoing. Attempts to mitigate this risk of increased legal exposure will ultimately increase the length of the auditor's report while only providing minimal incremental benefits to investors at best. As with many new disclosure requirements, it is likely that in this situation companies and auditors will develop a minimalist approach to disclosure, so as to reduce legal exposure. This new "boilerplate" will not benefit any investors. The risk of legal exposure, however, is not limited only to the company; auditors will also face significant risks if their disclosure deviates in any meaningful way, or highlights different areas, from the company's and therefore they may choose to duplicate the company's reporting as much as possible. This creates an incentive for redundant and repetitive disclosure, rather than producing any meaningful insight for investors. This could also lead to over-reporting of CAMs, including CAMs related to areas not disclosed by management, as auditors seek to manage their own legal exposure.

The potential for conflicting disclosure is exacerbated by the expansive scope under the Proposed Standard that an auditor must consider when contemplating whether any matter is a CAM. The Proposed Standard states that a CAM may arise from "any matter arising from the audit of the financial statements *that was communicated or required to be communicated* to the audit committee" (emphasis added). By setting the boundary at not just matters that are "required to be communicated" but at any matter that is communicated to the audit committee, *whether or not required*, a company may decide to limit communications to only that which is strictly required under the applicable financial reporting framework. This chilling of communications between management and their auditor will prevent the auditor from receiving the benefit of background or other contextual information that better informs the audit team, which would lead to a more comprehensive audit. While we acknowledge that, as the PCAOB points out, the current scope of matters required to be communicated under the applicable existing frameworks is quite extensive, we do not agree with the PCAOB's conclusion that "there may be few, if any, relevant communications affected." If the relevant parties are aware that any communication may form the basis for a conclusion regarding a CAM, then parties necessarily will shape their communications in response to this possibility. Even if the overall engagement between the company and its auditor does not change, it is unavoidable that the tone and tenor of such engagement will change as a result of the Proposed Standard.

Finally, we would also point out that the Proposed Standard's guidance that "[i]t is expected that, in most audits, the auditor would determine that at least one matter involved especially challenging, subjective, or complex auditor judgment" is not helpful in that it would seem to imply that an auditor should, at the bare minimum, identify at least one matter that could be a CAM. Such guidance could pressure auditors to identify CAMs which would not otherwise be disclosed.

Conclusion

While we support the PCAOB's objective to improve the relevance and usefulness of the auditor's report, we do not believe the provisions regarding CAMs achieve this objective and accordingly we urge the Commission to carefully consider the concerns we and others have identified prior to implementing any new standards. The Proposed Standard has a laudable goal of improving the usefulness of the audit report for all investors by trying to address information asymmetries that may exist between investors and auditors, but we question the manner by which the PCAOB has sought to address it. We believe the Proposed Standard will likely result in more, but less useful, information that will do more to harm rather than inform investors. The addition of the CAM process will also result in significant additional costs to shareholders given the extra time and resources required to meet the requirements from the auditor and the company.

We appreciate the opportunity to express our views and concerns regarding the Proposed Standard. If you have any questions regarding our response, or would like to discuss our comments further, please call me at [redacted].

Sincerely,

Robert A. Klug
Vice President, Corporate Controller and Chief Accounting Officer

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