

# P B T K

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February 16, 2012

Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, N.W.  
Washington, D.C. 20006-2803

Transmitted by e-mail to: [comments@pcaobus.org](mailto:comments@pcaobus.org)

Re: PCAOB Rulemaking Docket Matter No. 030

We are pleased to respond in this letter to the Board's reproposed standard (RS) entitled *Communications with Audit Committees* that is contained as Appendix 1 to its Release No. 2011-008 (the Release) of December 20, 2011. We previously responded briefly (Comment Letter No. 23) on May 28, 2010, to its earlier proposal issued March 29, 2010, in Release No. 2010-001. Our comments that follow are consistent with those made earlier.

As we stated in our response to the 2010 proposal, we agree in principle with the objectives of auditor communications with audit committees, as now set forth in the second paragraph of Part I of the Release; however, we continue to find the overall tone of the RS (as suggested in the comments of many others in response to the Board's earlier proposal) to be largely one of misplaced responsibility, *i.e.*, inappropriately shifting primary responsibilities for communicating (or inquiring) about certain matters from management (or the audit committee) to the auditors. A similar view is expressed in the excellent letter of January 10, 2012, from the distinguished Prof. Dennis R. Beresford (Comment Letter No. 1), who writes from the perspective of an audit committee member. Prof. Beresford wisely states (among other things with which we strongly concur) that the RS "does not acknowledge the proper roles of the auditor and management in certain key respects." Perhaps this phenomenon results from the practical reality that only auditors are subject to the regulatory control of the PCAOB.

Our specific responses to the seven questions posed by the Board in the Release are contained in the attachment. Our overarching concerns, however, are set forth in detail in the following five paragraphs, which are numbered to facilitate referencing, where applicable, from the responses in the attachment.

1. We believe it clearly should be management's primary responsibility, not the auditor's, to inform the audit committee of accounting and other matters involving the financial statements, rather than the audit process, including but not limited to "significant unusual transactions that are outside the normal course of business," the effects of management's decisions regarding the selection of accounting methods from available alternatives, methods used for accounting estimates, and sensitivity of estimates to changes in assumptions. Many such matters are typically disclosed in management's discussion and analysis drafts of which ordinarily should be reviewed by audit committees prior to filing with the SEC. Except as necessary to comply with the requirements of Rule 2-07 of Regulation S-X (see paragraph 4, below), auditors otherwise may rightfully be required to comment supplementally on management's communications to the audit committee if necessary. However, the auditor's communication responsibilities to the audit committee regarding such matters should always be secondary to management's.
2. Although we believe the audit committee rightfully should have a responsibility to assess and continually reassess the auditor's professional competency, the committee should not be encouraged to second guess audit strategy and scope decisions (including with respect to staffing), which should

remain primarily the responsibility of the auditor. We believe mandatory, proactive auditor communications about matters of audit scope, regardless of the required level of detail, would likely have the effect of inappropriately encouraging such second-guessing by audit committees. Rather, auditors should remain prepared to react responsively to appropriate questions about audit strategy and scope from audit committees but only to the extent, in the auditor's sole judgment, that the effectiveness of the audit process is not compromised. Accordingly, we believe the final standard should contain cautionary language to this effect regarding audit committee communications of matters of audit strategy and scope, which language should emphasize the need for auditors to guard against allowing such communications to present exposure to the risk of circumvention by management. Such language (regarding client access to engagement documentation) is contained in the Auditing Standards Board's AU sec. 339.31 but was not retained by the PCAOB when it was superseded by AS 3.

3. We believe a standard should encourage auditors to strive to preserve an ability (a) to evaluate objectively the effectiveness with which management and the audit committee interact and communicate with one another, and (b) to report perceived weaknesses in the process, and (c) to address such weaknesses appropriately in setting audit scope. However, we firmly believe that, like that of its predecessor proposal, the tone of the RS puts the auditor in the position of inappropriately attempting to regulate audit committees by telling them what the PCAOB thinks they should want to know. We see this as attempting to patch a weakness perceived in the performance of audit committees that results from a lack of regulatory pressure thereon from a more appropriate source such as the SEC. Except when seen as directly and significantly affecting the reporting entity's internal control over financial reporting, it should not be the auditor's responsibility to dictate to audit committees what they should be interested in to further the effectiveness of their oversight objectives (nor should it be the responsibility of those who set auditing standards). They should, however, report perceived weaknesses in the oversight process to the extent they are seen as deficiencies in internal control over financial reporting.
4. The Release makes several references (specifically, in paragraph 2 of Appendix 4 thereto and in several footnotes) to the SEC's Rule 2-07 of Regulation S-X (17 CFR 210.2-07), but the text of the RS, itself, does not. Several terms used in Rule 2-07 that are derived and used *verbatim* (and without explanation) from SOX Sec. 204 are unclear. We believe the utility of a final standard on audit committee communications would be substantially enhanced by including supplemental guidance that would appear within its text (or an appendix) as to the meaning of such vague and imprecise terms and otherwise as necessary to enable consistent compliance with Rule 2-07. For example, the term, "discussed with management," is a qualifying term used to determine when Rule 2-07 applies to communicating alternative accounting policies practices available under generally accepted accounting principles. Guidance as to meaning of "discussed with management" should also be made applicable when the term is used with respect to pre-appointment/retention issues now contained in paragraph 4 of the RS. In addition, the standard should contain a clear definition of what is meant by the term, "critical accounting policies," and an explanation of what is meant by the term, "to be used," with respect thereto. Moreover, guidance provided by the SEC in 2003 in its Release 33-8183 as to the content of certain communications required by Rule 2-07 is not readily accessible by many practitioners and should be included in the standard.
5. Lastly, we agree with Prof. Beresford that the final standard should not permit auditors to comply with only oral communications, as provided in paragraph 24 of the RS. Oral communications are too likely to be misunderstood (or even denied).

Thank you for this opportunity to comment. Once again, we hope the Board finds our comments useful in its deliberations on this important matter. Please contact the undersigned at [hlevy@pbt.com](mailto:hlevy@pbt.com) or 702/384-1120 if there are any questions about these comments.

Very truly yours,  
Piercy Bowler Taylor & Kern, Certified Public Accountants



Howard B. Levy, Principal and Director of Technical Services  
Attachment

**Q1.** *Are the communication requirements in the new proposed standard appropriately aligned with the performance requirements in the risk assessment standards, where applicable? If not, why?*

**A1.** No. For reasons set forth in paragraph 2 of this letter, we do not believe auditors should be required to be proactive in discussing their risk assessments and other scope judgments with audit committees, but rather they should limit such discussions to responses to direct questions and only to the extent that, in the auditor's sole judgment, the effectiveness of the audit process is not compromised.

**Q2.** *The communication requirements included in the new proposed standard are based on the results of procedures performed during the audit. Are there additional matters that should be communicated to the audit committee that also are based on existing auditor performance obligations?*

**A2.** No. We believe there already are sufficient audit committee communication requirements in current standards relative to "results of procedures performed during the audit," as we would interpret that term or a similar term such as "results of the audit." (Neither term is defined in Appendix A to the RS.) This question, however, incorrectly asserts that the RS would limit required communication to those "based on results of procedures performed" when, in fact (and inappropriately, in our opinion, in many instances), the RS reaches far beyond such a limit. Moreover, paragraphs 12-16 of the RS deal with matters that, although quite likely to have come to the auditor's attention during the audit, and perhaps appropriate for auditors to comment upon in audit committee communications, are not appropriately characterized, in our view, as "results" of audit procedures performed.

**Q3.** *The auditor is required to have the engagement letter executed by the appropriate party or parties on behalf of the company. If the appropriate party or parties is other than the audit committee, or its chair on behalf of the audit committee, the auditor should determine that the audit committee has acknowledged and agreed to the terms of the engagement.*

**a.** *Is the requirement in the standard clear?*

**A3a.** Yes. However, in the event the engagement letter is executed by management rather than the audit committee or its chair (as would be permitted under paragraph 6 of the RS), we believe the letter should contain management's representation of its authority to engage the auditor on behalf of the committee, and it should be management's responsibility to provide the engagement letter to the audit committee and the committee's responsibility (or its chair's) to notify the auditor in the event it takes exception thereto.

**b.** *As stated, the new proposed standard allows the acknowledgment by the audit committee to be oral. Should the acknowledgment by the audit committee, or its chair on behalf of the audit committee, be required to be in a written form or is oral acknowledgment sufficient?*

**A3b.** As noted in A3a, above, we do not believe the final standard should contain a mandatory or presumptively mandatory requirement for an auditor to obtain any positive acknowledgement of agreement by the audit committee, but if such an acknowledgment were to be required, we believe it should be in writing even if only indirectly such as in the committee's minutes (if available timely). Whatever is the Board's final position on the form of acknowledgment, however, we believe it should be presented in the body of the final standard (near what is now paragraph 6 of the RS) and not merely in an appendix as it now appears.

**Q4.** *Is the requirement for the auditor to communicate significant unusual transactions to the audit committee appropriate? If not, how should the requirement be modified?*

**A4.** No. For reasons set forth in paragraph 1 of this letter, we do not believe auditors should be required to be proactive in reporting significant unusual transactions to audit committees, as set forth in paragraph 14 of the RS, but rather they should limit their audit committee communications on such matters to commenting on management's reports to the audit committee about such matters. (See A5, below.)

- Q5.** *Is the requirement appropriate for the auditor to communicate to the audit committee his or her views regarding significant accounting or auditing matters when the auditor is aware that management has consulted with other accountants about such matters and the auditor has identified a concern regarding these matters? If not, how should the requirement be modified?*
- A5.** No. Paragraph 12 the RS states that “if management communicates matters related to accounting policies, practices, and estimates to the audit committee, the auditor does not need to communicate these matters at the same level of detail as management as long as the auditor (1) participated in management's discussion with the audit committee, (2) affirmatively confirmed to the audit committee that management has adequately communicated these matters, and (3) identified for the audit committee those accounting policies and practices that the auditor considers critical. The auditor is required to communicate any omitted or inadequately described matters to the audit committee.” However, we believe such language should be expressed positively as the preferential form of communication (the “default,” if you will, *i.e.*, management reports; auditor comments), not merely an acceptable second choice alternative. Moreover, as we stated in paragraph 1 of this letter, we believe such language should be extended to clearly apply to substantially all accounting matters and others involving the financial statements.
- Q6.** *Are the amendments to other PCAOB standards appropriate? If not, why?*
- A6.** We have not undertaken to respond to this question.
- Q7.** *The Board requests comments regarding the audits of brokers and dealers on the following matters:*
- a.** *Whether the communication requirements under the Board's interim standard, AU sec. 380, should be applicable to audits of brokers and dealers if audits of brokers and dealers are to be performed under PCAOB standards before the new proposed standard becomes effective? If so, should it be applicable to audits of all brokers and dealers?*
- A7a.** No. We believe the financial oversight responsibilities of audit committees or their equivalents are, and should remain, intended to serve the needs of public holders of equity interests and that auditor communications have been, and should continue to be, intended primarily to assist such committees in meeting such responsibilities, rather than to assure that auditors obtain information from the committees to aid them in scope determination (which objective we believe would be met without such a standard). Accordingly, we do not believe the requirements of either the current interim standard, AU sec. 380, or the RS should be deemed applicable to securities broker-dealers that are not issuers.
- b.** *Whether the auditor's communications to audit committees included in the new proposed standard should be applicable to all audits of brokers and dealers?*
- A7b.** No. See A7a, above.
- c.** *Are there any communication requirements specific to audits of brokers and dealers that should be added to the new proposed standard? Alternatively, are there any communication requirements contained in the new proposed standard that should not be applicable the audits of brokers and dealers? If so, provide examples and explanations for why the communication requirements for audits of brokers and dealers should be different from other audits covered by the new proposed standard.*
- A7c.** No. See A7a, above.