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Office of the Secretary
Public Company Accounting Oversight Board
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Re: PCAOB Rulemaking Docket Matter No. 30, *Proposed Auditing Standard Related to Communications with Audit Committees; Related Amendments to PCAOB Standards; and Transitional Amendments to AU sec. 380*

Dear Board Members and Staff:

We appreciate the opportunity to comment on the Public Company Accounting Oversight Board's (PCAOB or Board) *Proposed Auditing Standard Related to Communications with Audit Committees; Related Amendments to PCAOB Standards; and Transitional Amendments to AU sec. 380*, and we respectfully submit our comments and recommendations thereon. In consideration of the responsibilities instilled upon the audit committee by the Sarbanes-Oxley Act of 2002, the increasing complexity of financial accounting standards, the significant changes in recent industry and market conditions, and the call from investors for high quality financial reporting, audit committees are becoming more accountable and their oversight responsibilities more demanding. We believe that empowering audit committees with the necessary information and training to effectively perform their responsibilities is a critical component of maintaining and enhancing investor protection.

Although audit committees need to obtain and evaluate information from a variety of sources to meet their objectives, the communications between the audit committee and the auditor are essential for audit committees to oversee the financial reporting process and the auditor's work and for auditors to perform an effective audit. Accordingly, we support the Board's initiative to clarify and strengthen these two-way communications based on the relative importance of the matters to be communicated throughout the audit, including encouraging more open, constructive dialogue and less formal, standardized reports. Overall, we believe that the proposed auditor considerations and requirements are appropriately aligned with the risk assessment standards; however, we suggest that the standard include considerations around the scalability of the communications to reflect circumstances such as the entity's governance structure and the audit committee's knowledge and familiarity with the entity and its auditor.

Significant issues discussed with management as to auditor's appointment

Paragraph 4 of the proposed standard requires the auditor to discuss with the audit committee any significant issues discussed with management in connection with the appointment or retention of the auditor, including significant discussions regarding the application of accounting principles and auditing standards. Because the audit committee is now responsible for the appointment, compensation, and oversight of the auditor, this requirement may seem contradictory to that responsibility. Appendix 4 of the PCAOB's release indicates that the requirement was retained "…because the audit committee might ask management for its views concerning the appointment or retention of the auditor based on the interaction between the auditor and management." It goes on to indicate that "…management's views might be influenced by the auditor's evaluations and conclusions regarding the application of accounting principles or auditing standards."

To appropriately reflect these views, the audit committee would need to make certain inquiries of both management and the auditor, which would assist the audit committee in making an informed judgment. That said, we believe that a more appropriate requirement would be for the auditor to discuss with the audit committee significant issues related to the entity's accounting and financial reporting practices or management's integrity that were considered by the auditor during its client acceptance or retention process that have not already been communicated via the other requirements in the proposed standard. This approach would emphasize the audit committee's role as the decision-maker in accepting or retaining the auditor.

Establish an understanding of the terms of the audit

We agree with superseding AU sec. 310, *Appointment of the Independent Auditor*, and including requirements, within the proposed standard, related to the auditor's responsibility to establish an understanding of the terms of the audit engagement with the audit committee. In addition, we generally agree with the requirements in the proposed standard to provide the engagement letter to the audit committee annually, have the engagement letter executed by the appropriate parties on behalf of the entity, and determine that the audit committee has acknowledged and agreed to the audit engagement terms. We note, however, that the Board's interpretations of these requirements are included within Appendix 4 of the release, which may be lost upon finalizing the proposed standard. As with previous proposals, we request the Board to include relevant interpretations related to the application of the requirements within the standard itself or modify the requirements themselves to be clearer. It is possible that some firms may not interpret the Board's requirements in the same fashion without this additional discussion, particularly the nuance between *providing* and *preparing* the engagement letter annually and the *written* or *oral* audit committee acknowledgment.

The Board requested specific comments as to whether the audit committee's acknowledgement should be in written form or whether oral acknowledgment is sufficient. In light of the audit committee's responsibilities instilled upon it by the Sarbanes Oxley Act of 2002, we prefer a written acknowledgment, whether it is included within the engagement letter itself or within the minutes of the audit committee's meeting. An oral acknowledgement seems to weaken the spirit of the law and the audit committee's related responsibilities. Further, in circumstances in which the engagement letter is executed by the audit committee, we believe that the auditor should determine that management has also acknowledged and agreed to the terms of the audit engagement, in particular management's responsibilities and the auditor's related expectations.

Obtaining information relevant to the audit

Paragraph 8 of the proposed standard includes a rather broad requirement for the auditor to inquire of the audit committee whether it is aware of matters that might be relevant to the audit; it also provides and references certain matters that are to be included within these inquiries. We generally agree with the requirement and the Board's intent not to limit the nature of the auditor's inquiries of the audit committee, but we also believe that the requirement could be further clarified by providing some context regarding matters relevant to the audit from an audit committee perspective. In this regard, it may be helpful to provide audit committees with some guidance as to what this inquiry entails and what is expected to be communicated to the auditor. It may also be appropriate to include, as part of these inquiries, the audit committee's awareness of significant company events and transactions or significant changes in company conditions or activities. Such inquiry would assist the auditor in confirming their understanding of the entity and its environment. This would be incremental to the inquiries required by the risk assessment standards.

Accounting policies, practices, and estimates

We support the changes the Board made from the previous proposal to clarify the nature and extent of the communication requirements related to accounting policies, practices, and estimates, including the clarifications made with regard to management's communications of these matters. However, we believe that the auditor's communications should be flexible to take into account the audit committee's knowledge of and familiarity with the entity and its auditor, including whether the audit is an initial or continuing engagement. Although the additional discussion in Appendix 4 recognizes that the discussion could vary from year-to-year, the proposed standard, as written, seems more prescriptive. We recommend that the Board include an additional note within the proposed standard that will more clearly allow the auditor to vary the communications based on engagement circumstances.

Significant unusual transactions

The Board requested specific comments with regard to the communication requirements related to significant unusual transactions. We believe that it is appropriate to discuss such transactions with the audit committee. However, management should have the primary responsibility for communicating such transactions, including their business rationale, to the audit committee. As such, we believe that the note at the end of paragraph 12, which would allow the auditor to communicate information that was omitted by management or inadequately described by management to the audit committee, should also apply to this communication.

Audits of brokers and dealers

We understand and agree with the transitional amendments to AU sec. 380, *Communication With Audit Committees*, particularly eliminating the last sentence in paragraph .01 and footnote 2, which could be interpreted that the standard does not apply to audits of brokers and dealers. We also agree with aligning the effective date of these amendment with the effective date of the

U.S. Securities and Exchange Commission's (SEC) amendments related to audits of brokers and dealers, if such amendments become effective prior to the proposed standard.

Further, we concur that the proposed standard should apply to audits of brokers and dealers and do not believe that there are any additional requirements that would need to be included from a financial statement audit perspective. Any additional communication requirements related to other services, such as the proposed examination or review engagement, should be included within those standards. We do, however, ask that the Board consider the following matters to make the communication requirements more scalable to audits of non-issuer brokers and dealers:

- The Board appropriately recognizes various governance structures that are permitted by regulation and may exist for brokers and dealers. In particular, the additional discussion in Appendix 4 indicates that "…in an owner-managed entity, the designated person would be the owner." It further indicates that in a limited partnership, "…the designated person may be the managing or general partner responsible for preparation of the financial statements." We believe that if those charged with governance and management are the same individuals, some of the communications would not apply. Thus, it would be appropriate for the final standard to provide additional clarification in this regard, thereby allowing the auditor to adapt the communications based on the governance structure.

- Non-issuer brokers and dealers are currently not subject to the SEC's independence requirements related to audit committee communications regarding critical accounting policies and practices and critical estimates (Rule 2-07 of Regulation S-X), nor do brokers and dealers disclose such matters in a Management's Discussion and Analysis. However, the proposed standard incorporates similar communication requirements that would be applicable in audits of brokers and dealers. We recognize that the proposed standard defines these terms; yet, management of brokers and dealers are not required to differentiate between matters that are significant versus those that are critical within the financial statements. Since separate disclosures are not provided, the auditor may be unable to effectively make the separate assessment required by paragraph 13b. As such, we believe that this is an area in which the requirements for issuers and non-issuers may need to differ or require more clarification. Refer to our specific comments on paragraphs 13b-c below.

Potential additional communication requirements

We believe that, in connection with the Board's transparency initiatives and its initiatives to enhance auditor independence, objectivity, and professional skepticism, the Board may consider additional communication requirements related to the acceptance and retention of the auditor. These communications could include matters related to the firm's internal quality-control procedures and inspection issues raised during the most recent PCAOB inspection. We support consideration of these communications to further enhance the audit committee's oversight. In this regard, we encourage the PCAOB, in conjunction with the SEC, to further strengthen these responsibilities by providing guidance to audit committees to assist them in effectively performing their role and also looking at potential avenues to monitor audit committee involvement when reporting issues arise.

Amendments to PCAOB standards

We propose that the Board consider the effective date in regard to the amendments to AU sec. 722, *Interim Financial Information*, to permit sufficient time for implementation of the new requirements.

Other comments

The following offers more specific comments related to certain paragraphs and Appendix C for the Board's consideration.

Paragraph	Comment
1, 3	The proposed standard imposes certain responsibilities on the auditor to *obtain* information relevant to the audit from the audit committee. We agree with this notion, but suggest that the proposed standard refer to the auditor's responsibilities to *request* such information, as the auditor cannot control what the audit committee provides. A scope limitation would then be imposed if the audit committee did not provide the requested information.
10d	Until such time the Board amends AU sec. 543, *Part of Audit Performed by Other Independent Auditors*, it may be more appropriate to align the audit committee communication requirements in this paragraph with the requirements therein. For instance, the principal auditor could communicate the names and locations of other auditors, the components upon which they will perform audit procedures for purposes of the principal auditor's audit, and whether the principal auditor will assume responsibility or make reference to the work of the other auditor. If the Board decides to maintain the requirement as proposed, we suggest clarifying what is intended by the reference to the *scope of audit procedures* in consideration of the note to paragraph 9.
13b-c	These paragraphs require the auditor to communicate to the audit committee the auditor's assessment of management's disclosures related to critical accounting policies and practices, along with any significant modifications to the disclosures proposed by the auditor, and the basis for the auditor's conclusions regarding the reasonableness of critical accounting estimates. For issuers, we believe that this would include matters included or disclosed in the financial statements, as well as those in Management's Discussion and Analysis. Accordingly, a reference to the requirements of Rule 2-07 of Regulation S-X seems warranted, as PCAOB standards are more limited with regard to the auditor's responsibilities for other information included in Management's Discussion and Analysis.
13d	We understand the purpose of this communication as it relates to the auditor's evaluation of whether the financial statements achieve fair presentation. However, the requirement, as written, could be considered duplicative in regards to the communications of corrected and uncorrected misstatements and departures from the standard auditor's report, both of which would apply if the financial statements did not conform with the applicable financial reporting framework. As such, it is not fully clear what the auditor is expected to communicate and at what threshold. It is our view that the auditor could communicate significant matters resulting from the auditor's evaluation, such as modifications that were necessary to the overall presentation, structure, and content, including disclosures, so that the financial statements would not be misleading.
13e, 13h	These communications, which pertain to consultations and material written communications, are included under the broad category of communications related to the auditor's evaluation of the quality of the company's financial reporting. We suggest that the Board reconsider the placement of these communication requirements within the proposed standard. With respect to communicating consultation matters, we believe that it would be helpful to include a note within the final standard that further clarifies the Board's intent regarding the matters to be communicated, such as the paragraph describing the differences between a difficult and a contentious issue within the additional discussion in Appendix 4.

Paragraph	Comment
15	This paragraph essentially retains an existing requirement for the auditor to communicate the auditor's responsibilities related to other information, any related procedures performed, and the results thereof. Typically, except when material inconsistencies or misstatements of fact are identified, the communication is rather boilerplate because the auditor describes those responsibilities and procedures as set forth by professional standards. In reading the Board's additional discussion in Appendix 4, it appears that the Board intends the auditor to describe all of the procedures the auditor performed on the information. We believe that this is a nuance that will likely be missed and also that any description of additional procedures could inappropriately convey a level of assurance that is not being expressed. Accordingly, we recommend that the final standard require the auditor to communicate the auditor's responsibilities related to other information and any identified material inconsistencies or misstatements fact, including the auditor's response to such matters. We believe that such communication would be more relevant to the audit committee.
16	The Board requested specific comments as to the appropriateness of the requirement for the auditor to communicate significant auditing or accounting matters that were the subject of management consultations with other accountants about which the auditor has concern. We agree with the revised requirement, as we believe that it allows for appropriate auditor judgment based on the significance of the matters and the auditor's concerns about such matters.
25	To communicate matters in a timely manner, the note to this paragraph allows the auditor to communicate only to the audit committee chair. However, it also indicates that the auditor should communicate such matters to the *full* audit committee *prior to the issuance of the auditor's report*. As currently worded, the proposal does not address all situations in which the auditor may need to only communicate to the audit committee chair to meet the requirements in the proposed standard. For example, the auditor would be required to provide to the audit committee the representation letter and the uncorrected misstatements attached thereto as well as the wording of the auditor's report when the report is modified or otherwise includes explanatory language. However, the date of the auditor's report aligns with the date of the management representation letter, which, in most case, also aligns with the date of issuance of the auditor's report. In this case, providing these matters to the audit committee chair and allowing him or her to distribute the information to other audit committee members should be sufficient. The communications with the audit committee prior to the issuance of the auditor's report could include draft copies, in addition to the related discussion.
Appendix C	Appendix C to the proposed standard describes the matters that are to be included in the audit engagement letter. Although we do not have significant reservations related to these matters, we do have some recommendations for the Board. In some respects, Appendix C seems to provide specific language to be included in the engagement letter as it relates to the auditor's responsibility. Although we recognize that this may not be the intent, due to various situations that may arise, including compliance with multiple standards, it may be best to simply identify the matters that should be included. In addition, the matters related to the communication of significant deficiencies and material weaknesses seem overly prescriptive in light of the auditor's other communication responsibilities.

We would be pleased to discuss our letter with you. If you have any questions, please contact Karin A. French, National Managing Partner of Professional Standards, at (312) 602-9160.

Sincerely,

Grant Thornton LLP