May 28, 2010

Office of the Secretary
Public Company Accounting Oversight Board
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Re: PCAOB Rulemaking Docket Matter No. 030, *Proposed Auditing Standard Related to Communications with Audit Committees, and Related Amendments to Certain PCAOB Auditing Standards*

Dear Board Members and Staff:

We appreciate the opportunity to comment on the Public Company Accounting Oversight Board's (Board or PCAOB) *Proposed Auditing Standard Related to Communications with Audit Committees, and Related Amendments to Certain PCAOB Auditing Standards.* As a member of the Center for Audit Quality (CAQ), we participated in the drafting of the CAQ's letter of comment in response to the proposed standard. On an overall basis, we support the comments in the CAQ's letter but wish to separately provide our comments and recommendations, including our responses to the Board's specific questions.

We support the Board's desire to enhance and emphasize the importance of effective two-way communications between the auditor and the audit committee. Not only are effective two-way communications an essential component of an audit, they are necessary for the audit committee to achieve its oversight responsibilities to protect the public interest. However, we believe that the prescriptive nature of the proposed standard, particularly as it relates to communicating significant and critical accounting policies and practices, will have the unintended consequence of less effective communications. We agree that many of the matters to be communicated are appropriate, relevant, and useful to the audit committee, but the Board must clearly distinguish the auditor's responsibilities from those of management and the audit committee. It is not feasible or appropriate to require the auditor to communicate all of the matters listed on every audit and review engagement, particularly when the communication responsibility primarily rests with management. This approach may lead to rote communications that have the effect of obfuscating more critical discussion points.

We continue to support the need for the Board to conform to the extent possible to the standards established by the International Auditing and Assurance Board (IAASB) and to consider the work of the Auditing Standards Board (ASB) of the American Institute of Certified Public Accountants. We believe that maintaining consistency with the standards of the

IAASB and ASB, while also addressing the particular needs of issuers, enhances the effectiveness, quality, and uniformity of audits.

Objectives of the auditor

The following includes our responses to the Board's specific questions related to the auditor's objectives. Overall, we are supportive of the proposed objectives. Nevertheless, we have a few recommendations that we believe will further clarify the auditor's responsibilities.

1. Are the objectives of the auditor in the proposed standard appropriate? If not, why? Should other matters be included in the objectives?
   For the most part, we believe that the objectives of the auditor in the proposed standard are appropriate. However, similar to International Standard on Auditing (ISA) 260, *Communication with Those Charged with Governance*, we suggest including an additional objective for the auditor to obtain from the audit committee information that is relevant to the audit. We believe this objective is necessary for the auditor to recognize the importance of, as well as to promote, effective two-way communications with the audit committee. The objective would also provide a basis for the auditor's evaluation of the adequacy of such communications. Further, although the Board recognizes the importance of inquiring of the audit committee in the release and includes a specific requirement to do so in the proposed standard, excluding the ISA objective from the proposed standard can imply that the Board believes that it is not an essential element of the audit. We note that the Board's views on this matter were not included in Appendix 3, which compares the proposed standard with the corresponding standards of the IAASB and ASB.

2. Are the objectives adequately articulated? Should the articulation of the objectives focus on the outcome that should be achieved by performing the required procedures?
   We prefer aligning the language used in the objectives with ISA 260. Although the objectives stated in the proposed standard are outcome based, we believe the way they are articulated could be clearer and more practical, as discussed further in our response to question 6. Also, the ISA objectives are relevant to issuers and non-issuers alike, and we see no need to depart from those objectives. However, in clarifying the objectives in the proposed standard, we suggest the following revisions:

   - Referring to the "overall" audit strategy in paragraph 3(b) to refine the auditor's responsibilities and address the concerns expressed in our response to question 6.

   - Referring to the "oversight of the company's" financial reporting process in paragraph 3(c) to be clear that the auditor's communications are focused on matters that are important to merit the audit committee's attention, thereby encouraging more meaningful discussions.

   - Using the phrase "to support the opinion to be expressed in the auditor's report" in lieu of the phrase "to support the objectives of the audit," to more clearly indicate that ineffective communications do not provide the auditor with sufficient appropriate audit evidence to form an opinion.

Establish a mutual understanding of the terms of the audit

We concur with the elimination of AU sec. 310, *Appointment of the Independent Auditor*, and the inclusion of the requirements to establish a mutual understanding of the terms of the audit engagement together with the auditor's other audit committee communication responsibilities. The following includes our responses to the Board's specific questions related to the use of an audit engagement letter.

3. Is it appropriate for the proposed standard to require that an engagement letter be prepared annually? If not, why?

   In consideration of the audit committee's oversight responsibilities, including the appointment and retention of the auditor, we believe it is appropriate for the auditor to establish a mutual understanding of the terms of the audit engagement on an annual basis. However, in consideration of this question and the statements made in the release, it is not clear whether the Board intends to require a new engagement letter on an annual basis. Today, there are alternative methods (for example, an "evergreen letter") for establishing such an understanding that would seem to meet the proposed requirement. The Board should clarify its views on this matter within the proposed standard.

4. Are there other matters that would enhance investor protection that should be added to an engagement letter? If so, what other matters should be included in an engagement letter?

   In addition to the auditor's and management's responsibilities, we believe that the engagement letter, for an audit and a review of interim financial information, should include the audit committee's responsibilities to provide the auditor with information relevant to the audit (see our response to question 22). We also believe it is equally important for management to acknowledge the terms of the audit engagement, as the primary responsibility for the financial statements rests with management.

   With respect to Appendix C, which includes matters required to be communicated in the audit engagement letter, we have the following observations:

   - We believe it is not necessary for the engagement letter to include with such specificity the required auditor communications related to internal control deficiencies; although we acknowledge that this is an existing requirement. The inclusion of such information overshadows other key communications that are not required by the proposed standard to be included within the engagement letter.

   - We also believe that the audit engagement letter should include management's responsibility to provide unrestricted access to persons within the company from whom the auditor determines it necessary to obtain audit evidence. We consider this to be an important addition from ISA 210, *Agreeing the Terms of Audit Engagements.*

Obtaining information related to the audit

The following includes our response to the Board's specific question related to inquiries of the audit committee.

5. Is the proposed requirement to inquire of the audit committee appropriate? What other specific inquiries, if any, should the proposed standard include for the auditor to make of the audit committee?

   We support including a specific requirement to inquire of the audit committee about matters related to the audit within the proposed standard. We believe that the requirement would support the additional objective discussed in our response to question 1 for the auditor to obtain from the audit committee information that is relevant to the audit. However, we also believe the requirement needs to be placed in the appropriate context; otherwise, it seems overly broad and misplaced. In this regard, we propose the following:

   - Including within the proposed standard the analysis provided in Appendix 3 under "Obtaining Information Related to the Audit," which clearly indicates that the requirement "complements the requirement in the Proposed Auditing Standard, *Identifying and Assessing Risks of Material Misstatement*."

   - Clarifying that the inquiry pertains to other matters of which the audit committee is aware that would affect the overall audit strategy, including the scope, timing, and direction of the audit, to align the inquiry with the auditor's related communication in paragraph 9 of the proposed standard (see our response to question 6).

   - Including, as examples of other matters to inquire of the audit committee, the guidance provided by paragraph A14 of ISA 260, to the extent the guidance is applicable to audits of issuers and not otherwise addressed by PCAOB standards.

Overview of the audit strategy and timing of the audit

The following includes our responses to the Board's specific questions related to the auditor's communications of the overall audit strategy and timing of the audit.

6. Are the requirements to provide information on the auditor's audit strategy and timing of the audit appropriate? Does the auditor need more guidance related to the requirement to provide information on the auditor's audit strategy? If so, what type of guidance would be helpful?

   As proposed, we do not agree with the requirements in paragraphs 9 and 11 for the auditor to communicate to the audit committee matters related to the audit strategy and significant changes thereto. To meet the requirements in the proposed standard, the auditor would need to perform risk assessment procedures, identify significant risks, develop an appropriate response to those risks, and then hold discussions about these matters with the audit committee. Although this may seem reasonable to the Board, we are concerned that exhaustive communications related to the audit strategy and the auditor's risk assessments can compromise audit quality and effectiveness because the audit committee is not autonomous of management. Also, the communications are impractical. The proposed standard can only be complied with if the auditor and audit committee have multiple meetings scattered throughout the audit, including the one after the auditor's risk assessment. It is not feasible to mandate this on the auditor or the audit committee.

The Proposed Auditing Standard, *Identifying and Assessing Risks of Material Misstatement*, describes the "overall" audit strategy, which pertains to the planned scope and timing. We believe that communicating the overall audit strategy to the audit committee provides the appropriate level of communication. Also, we note that paragraphs A11 and A13 of ISA 260 provide useful guidance that could be included in the proposed standard to further clarify the nature of the communications. Further, our response to question 5 indicates that the required inquiry of the audit committee should relate to the auditor's communication of the overall audit strategy and that the inquiry could include the matters addressed in paragraph A14 of ISA 260. We believe that these changes to the proposed standard would strengthen the effectiveness of the two-way communications between the auditor and the audit committee.

With respect to paragraph 10, we question the need for the requirements to communicate certain specific matters, as proposed, on an annual basis for every engagement. For instance, it is very common for the auditor to utilize persons with specialized skill or knowledge on every audit engagement, such as an information technology specialist. Our view is that the audit committee may wish to be informed of the auditor's use of such persons in response to an identified significant risk, but not routinely on all engagements. We have the same view about the requirements in paragraphs 10(b) and 10(c) to communicate the auditor's consideration and use of the internal audit function, company personnel, or other third parties. Also see our response to question 7 regarding the communication requirements in paragraphs 10(d) and 10(e).

7. Is it sufficiently clear which types of arrangements should be communicated to the audit committee related to the roles, responsibilities, and locations of firms participating in the audit?

   Audit committees may not universally desire or need exceptionally detailed information of the sort that seems to be mandated by paragraph 10(d); therefore, we believe the auditor's communication should be limited to the fact that the auditor expects to use the work of other auditors. However, we also believe that the auditor's expected use of other auditors would be discussed in conjunction with the auditor's ability to serve as the principal auditor, which is a matter that the audit committee would need to consider prior to appointing or retaining the auditor as the principal auditor. Consequently, we suggest paragraphs 10(d) and 10(e), as proposed, be removed from the proposed standard in their entirety or further clarified. This aside, in response to the Board's question, the requirement to communicate the roles, responsibilities, and locations of firms participating in the audit is not clear without reading the release. We have previously suggested that the Board eliminate the practice of interpreting the requirements of its standards in the release. Although we find the Board's analysis helpful, information that is essential in applying the requirements, or requirements themselves, should be contained within auditing standards to help eliminate differences in practice.

Accounting policies, practices, and estimates

We have reservations regarding the communication requirements related to accounting policies, practices, and estimates. As stated in the release, a primary objective of the proposed standard is to "enhance the relevance and effectiveness of the communications between the auditor and the audit committee." We believe that simply including numerous additional requirements related to significant and critical accounting policies, practices, and estimates does not accomplish this objective.

Generally, many of the communication requirements relating to significant accounting policies and practices, as well those relating to critical accounting estimates, are the responsibility of management. We also believe that, in exercising effective oversight, the audit committee has a duty to proactively discuss these matters directly with management. Further, the audit committee should be familiar with the significant and critical accounting policies, practices, and estimates, as disclosed both in the company's financial statements and Management's Discussion and Analysis (MD&A). A well informed audit committee would enhance the quality and effectiveness of the two-way communications with the auditor, and consequently, the auditor's communications would pertain to the auditor's views on matters that are of utmost importance to warrant the audit committee's attention.

Although we recognize that, consistent with extant standards, the note in paragraph 12 allows the auditor to rely on certain management communications, we request the Board to reconsider the auditor's communication requirements in light of management's and the audit committee's responsibilities. The auditor need not be required to communicate matters that are to be communicated by management, nor accounting policies, practices, and estimates that are disclosed in the company's financial statements and MD&A. Focusing the requirements on the auditor's views regarding the quality of these matters could avoid boilerplate communications and prevent audit costs from rising, while promoting more meaningful and robust communications with the audit committee. Our responses to the Board's specific questions that follow provide more specific recommendations.

8. Are the proposed requirements regarding the auditor's communication responsibilities with respect to accounting policies and practices sufficiently clear in the proposed standard (e.g., is the difference between a critical accounting policy and a significant accounting policy or practice adequately described)?

   The proposed standard appears to be consistent with current requirements as they relate to the difference between a significant accounting policy and a critical accounting policy. However, in reference to our general comments above, we believe that the matters covered by the requirement in paragraph 12(a) should be communicated by management. Also, we do not understand the auditor's communication responsibility with regard to paragraph 13(b)(iii); particularly, the requirement is not clear with respect to what is expected to be communicated, how the auditor would consider anticipated future events in determining critical accounting policies and practices, and why this is relevant to the audit committee.

   With respect to paragraph 13(f), as drafted, we disagree with the requirement to communicate significant accounting matters where the auditor has consulted outside the engagement team. We are uncertain about the matters expected to be communicated in connection with this requirement. In addition, we believe the requirement will be difficult to operationalize because the nature and extent of consultations outside the engagement team that relate to accounting matters vary considerably. Although a consultation may relate to a significant accounting matter, the consultation per se may not be significant. Accordingly, if this requirement is to be maintained, we believe it should be limited to consultations with the national office, or a similar risk management function, on difficult or contentious financial reporting matters.

9. Is it helpful to include in the proposed standard the audit committee communications required by the SEC relating to accounting matters?
   Although the proposed standard appears to be consistent with the communication requirements in Rule 2-07(a)(1) and (a)(2) of Regulation S-X, the proposed standard does not include all of the requirements in the Rule. A statement that more clearly indicates that Rule 2-07 requires the auditor to communicate all critical accounting policies and practices, as well as certain other matters, may be useful in footnote 12 of the proposed standard. With respect to the communication of alternative treatments, we believe that a footnote referencing Rule 2-07(a)(2) should also be added to paragraph 13(e) of the proposed standard. Further, it is unclear, in consideration of the amendment to AU sec. 722, *Interim Financial Information*, whether the Board intends to extend the communication requirements related to critical accounting policies and practices to a review of interim financial information, as Rule 2-07 applies to an audit.

10. Is the definition of critical accounting estimates appropriate for determining which estimates should be communicated to the audit committee?
    We appreciate that the Board has defined a critical accounting estimate consistent with the U.S. Securities and Exchange Commission's (SEC) rules and regulations for disclosure in MD&A. A reference to those rules and regulations would further facilitate the auditor's understanding of what is expected to be communicated. The Board may consider working with the SEC to more clearly articulate the definition included in Appendix A of the proposed standard so that critical accounting estimates are distinctly differentiated from other material estimates in the financial statements. This may include incorporating previous SEC remarks on this matter.

11. Are the communication requirements regarding critical accounting estimates appropriate? If not, how should the proposed standard be modified to provide appropriate information to the audit committee?
    As previously mentioned, we believe that many of the communication requirements relating to critical accounting estimates are the responsibility of management, including communications regarding management's process and monitoring, significant assumptions, the reasons for any changes to assumptions, and the range of possible outcomes. The auditor can supplement management's communications by providing the audit committee with the auditor's views about the quality and reasonableness of management's selection, application, and disclosure of critical accounting estimates, as well as concerns regarding potential bias in management's estimates. We believe such communications would provide

more insight to the audit committee, as well as promote more effective communications with the auditor.

With respect to paragraph 13(c), we believe that the proposed standard should not require the auditor to communicate the auditor's evaluation of the reasonableness of management's process to develop critical accounting estimates and the basis for the auditor's conclusions regarding the reasonableness of those estimates. First and foremost, the auditor does not perform a separate evaluation of management's process or conclude on the reasonableness of a critical accounting estimate apart from the audit of the financial statements taken as a whole. Also, the communication requirement is redundant with other communication requirements. For instance, if management's process was not reasonable, the auditor may communicate, depending on how the matter is resolved, a control deficiency, a modification of the opinion, or a difficulty encountered in performing the audit. We believe that our recommendation in the previous paragraph would sufficiently address the matters in paragraph 13(c).

Management consultations with other accountants

The following includes our response to the Board's specific question related to management's consultations about accounting and auditing matters.

12. Should this requirement be expanded to include consultations on accounting or auditing matters with non-accountants, such as consulting firms or law firms?

We believe that the basis for requiring the communication related to management's consultations with other accountants about accounting or auditing matters primarily pertains to "opinion shopping" and the requirement in AU sec. 625, *Reports on the Application of Accounting Principles*, for the reporting accountant to consult with the continuing accountant. Although we believe it is management's responsibility to communicate the nature of the consultation to the audit committee, this is a significant matter where the auditor's views about the consultation need to be communicated. Therefore, we agree with maintaining the requirement in paragraph 15 of the proposed standard, provided the requirement is modified to require the communication of the auditor's views to the audit committee and to more clearly apply when the reporting accountant has consulted the auditor.

Although management's consultations about accounting or auditing matters with non-accountants would also be relevant to the audit committee's oversight of the company's financial reporting process, we believe that a separate requirement for the auditor to communicate such consultations is not necessary. Again, management should discuss these matters with the audit committee; however, there is no basis for determining that the auditor would be directly consulted about such matters or that the auditor would be aware of all management consultations with non-accountants. Further, if management consulted with non-accountants about an accounting or auditing matter of which the auditor is aware and that the auditor believes is significant to the audit committee's oversight of the financial reporting process, the auditor would be required to communicate the matter in accordance with paragraph 22 of the proposed standard. It would be appropriate for the auditor to communicate the auditor's views about management's use of third-party providers as it relates to significant or critical accounting policies and practices.

Going concern

The following includes our response to the Board's specific question related to the communications related to going concern.

13. Is the communication requirement on going concern clear? If not, how could the requirement be clarified?

    As currently drafted, we do not fully agree with the communication requirements related to going concern. We believe the requirement in paragraph 16(a) to communicate the conditions and events that indicate there could be substantial doubt about the company's ability to continue as a going concern, in addition to the information that mitigated the auditor's doubt, seems to be primarily based on paragraph .03a of AU sec. 341, *An Entity's Ability to Continue as a Going Concern*. Although this paragraph indicates that the auditor would perform additional procedures to obtain audit evidence that mitigates the auditor's doubt, it is unlikely that the auditor would come to a conclusion that the auditor's doubt is mitigated without considering management's own evaluation and plans, as contemplated by paragraph .03b of AU sec. 341. Accordingly, we believe that it is inappropriate to infer otherwise in paragraph 16(a) and that the requirement in paragraph 16(b), on its own, is sufficient.

    At this time, however, we suggest the Board either maintain the extant communication requirements or align those requirements more closely with ISA 570, *Going Concern*. This will provide the Board with additional time to consider the Financial Accounting Standards Board's standard setting activities in this area. We believe management's responsibilities related to the going concern assumption will become more transparent, and the auditor's responsibilities in AU sec. 341, including those relating to communications with the audit committee, will need to be aligned accordingly.

Corrected and uncorrected misstatements

The following includes our responses to the Board's specific questions related to the auditor's communication of corrected and uncorrected misstatements.

14. Are the requirements appropriate regarding the communications for uncorrected misstatements?

    Management has the primary responsibility for evaluating, quantitatively and qualitatively, the materiality of uncorrected misstatements and communicating its conclusions to the audit committee. We believe the requirement in paragraph 18 of the proposed standard for the auditor to also communicate to the audit committee the basis for the auditor's determination that uncorrected misstatements were immaterial (essentially, the auditor's concurrence with management's conclusions) is appropriate, except that we believe the communication of the qualitative factors considered by the auditor will become a boilerplate disclosure of the qualitative characteristics of materiality. We believe the auditor should be required to communicate such qualitative factors only if the auditor believes they are significant to the auditor's determination of immateriality and consideration of management's own conclusions.

Paragraph 18 of the proposed standard also requires the auditor to communicate corrected misstatements that might not have been detected except through the auditing procedures performed, including the implications such misstatements might have on the financial reporting process. We believe this requirement should be eliminated as it is duplicative of the auditor's required communications related to deficiencies in the company's internal control over financial reporting.

15. Should all corrected misstatements including those detected by management be communicated to the audit committee?

    We believe the Board should not require the auditor to separately communicate corrected misstatements detected by management. Depending on what the Board considers to be a corrected misstatement, the auditor may not be able to differentiate between adjustments made in the period-end financial reporting process and other journal entries to correct misstatements detected by management, and the auditor may not be informed by management of all such adjustments, which could number in the hundreds, if not thousands. If the Board receives feedback from audit committee members expressing their views that this information is essential to their oversight of the company's financial reporting process, we believe management, not the auditor, should have the responsibility to communicate such information to the audit committee.

Form and content of communications

The following includes our response to the Board's specific question related to the form and content of communications to the audit committee.

16. Like the existing standard, the proposed standard would allow the auditor to communicate many matters orally or in writing. Should the standard require that all or certain matters be communicated to the audit committee in writing? If only certain matters should be communicated to the audit committee in writing, what are those matters?

    We support the requirement in paragraph 23 of the proposed standard to communicate to the audit committee either orally or in writing. We believe it provides appropriate flexibility for the auditor to determine the form of communication, in consideration of the matters to be communicated and the audit committee's preferences. Also, requiring that certain matters identified in the proposed standard be communicated in writing may reduce the effectiveness of the two-way communications.

    Paragraph 23 also requires the auditor to document the communications, whether communicated orally or in writing, in sufficient detail for an experienced auditor, having no previous connection with the audit to understand the communications made. We believe the Board should clarify its expectations related to the auditor's documentation of the communications. For example, if the communications were made in writing, whether in a formal letter or a presentation, the requirement implies documentation beyond the written communication, whereas we believe the formal letter or presentation is sufficient to document the communication.

Timing

The following includes our response to the Board's specific question related to the timing of communications to the audit committee.

17. Are the requirements in the proposed standard on the timing of the auditor's communications appropriate? Should only certain matters be communicated annually? If so, which ones?

    For an audit of financial statements, we agree with the requirements to communicate to the audit committee in a timely manner, on an annual basis, and prior to the issuance (or release) of the auditor's report, provided the communication requirements are relevant to the current audit. The proposed standard should not impose requirements that would require the auditor to communicate the same matters from year to year, as also indicated in our response to question 6.

    With respect to reviews of interim financial information, we also agree that the communications should be made before the company files its interim financial information with the U.S. Securities and Exchange Commission (SEC). However, the extant standard recognizes that there may be practical difficulties in doing so and provides for such situations. We believe this may become even more prevalent based on the additional interim communication requirements imposed by the proposed standard in conjunction with the related amendment to AU sec. 722.

    In consideration of the additional requirements, we are further concerned that the interim communication requirements are ambiguous by merely referencing the proposed standard, which is written from the perspective of an audit. We acknowledge that proposed interim communication requirements are similar to the extant requirements and that guidance is provided with regard to the communication of "changes" during a review; however, we believe the interim communication requirements should be more transparent, particularly with respect to the requirements in a recurring and initial review. In this regard, the Board should take the opportunity to more clearly differentiate between the annual and the interim communication requirements, including the auditor's responsibility to evaluate the effectiveness of the two-way communications. It would be helpful to reference the specific paragraphs in the proposed standard that apply in a review of interim financial information.

    As a final matter, we bring to the Board's attention some inconsistencies between the proposed requirements and the release. The release includes additional requirements related to the timing of communications that are not included in the proposed standard. We believe that the Board should not use the release to further interpret the requirements. Also, the amendment to AU sec. 722 indicates that the communication for a review of interim financial information should be made before the company files its interim financial information with the SEC. The release, on the other hand, refers to a filing with a regulatory agency, such as the SEC. We are comfortable with the proposed requirement in the amendment to AU sec. 722. However, we believe the release could create issues for companies that may have filing deadlines with other regulatory agencies that do not coincide with the SEC filing.

Adequacy of the two-way communication process

The following includes our response to the Board's specific question related to the two-way communication process.

18. Does the requirement to evaluate the adequacy of the communication process promote effective two-way communications? Is more information on this requirement needed?

    The requirement to evaluate the adequacy of the communication process does not necessarily promote effective two-way communications. Nevertheless, we believe two-way communication is fundamental to an audit. Whether the audit committee is forthright in its communications to the auditor will influence the auditor's risk assessments and may also impair the auditor's ability to obtain sufficient appropriate audit evidence to form an opinion.

    We believe the requirements in paragraphs 26 and 27 of the proposed standard are sufficient, except with respect to the Note in paragraph 27. Although we acknowledge that the Note creates a link between the evaluation in paragraphs 26 and 27 of the proposed standard and the evaluation of the control environment in paragraph 25 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with an Audit of Financial Statements*, we believe the Note is not strong enough and could be further clarified. We believe the evaluation in paragraphs 26 and 27 directly influences the auditor's evaluation of the control environment, particularly as it relates to the effectiveness of the audit committee's oversight of the company's financial reporting process. The statement in the Note that the auditor "also should include the evaluation of the results of tests of controls related to the control environment regarding the audit committee" does not adequately describe the relationship between these requirements. For instance, we believe that the proposed standard should be clear that if the audit committee's communications to the auditor are ineffective, the auditor should consider this deficiency as it relates to the overall effectiveness of the audit committee's oversight of the financial reporting process.

    Further, under PCAOB standards, the auditor is required to communicate ineffective audit committee oversight to the board of directors, regardless of whether the auditor is performing an integrated audit or a financial statement only audit. Likewise, in a situation in which the auditor concludes that the two-way communications are not adequate, we believe the auditor should be required to communicate that conclusion to the full board of directors, rather than simply consider whether the communication is necessary, as currently required by paragraph 28.

Other communication requirements

The following includes our responses to the Board's specific questions related to the other communication requirements.

19. Are these other communication requirements appropriate and sufficiently clear? What other communication requirements should the proposed standard include, if any?

    We agree with the other communication requirements, except for the requirement in paragraph 14 related to other information. Although the requirement is consistent with extant standards, it could be modified to apply to audits of issuers. We believe the auditor should be required to only communicate identified material inconsistencies and material misstatements of fact and the adequacy of management's related response. The Board may also consider amending paragraph .05 of AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*, which currently requires the auditor to discuss material misstatements of fact with the "client," rather than the audit committee.

    With respect to the requirement in paragraph 19, we suggest the Board include a reference to paragraph .11 of AU sec. 508, *Reports on Audited Financial Statements*, which identifies the circumstances requiring an explanatory paragraph or other explanatory language in the auditor's report. We also recommend the Board obtain feedback from audit committees as to whether they believe it is necessary to obtain the proposed wording of the auditor's report in all circumstances, such as for consistency references or reporting on supplementary information. Many of the matters covered by paragraph .11 of AU sec. 508 are also addressed by other communication requirements in the proposed standard. In addition, the report may contain the same modifications from year to year.

20. Are the matters included as significant difficulties in paragraph 21 of the proposed standard appropriate? What other matters should be included as significant difficulties?

    Overall, we believe the matters identified as being significant difficulties in paragraph 21 of the proposed standard are appropriate. We suggest, however, that paragraph 21(e), which deals with management's unwillingness to make or extend its assessment of the company's ability to continue as a going concern, be addressed in conjunction with the requirements in paragraph 16.

21. Are any of the requirements included in the proposed standard inappropriate for auditors to communicate to audit committees based on the size or industry of the company under audit?

    Although the nature and depth of the communications may vary based on the type of company, the audit committee's interest and sophistication, and the circumstances of the particular engagement, the communication requirements in the proposed standard can be considered fundamentally appropriate, regardless of the company's size or industry. However, as previously expressed, we believe the proposed standard should not require the auditor to communicate all of the matters identified in the proposed standard for every engagement. Also, in revising the proposed standard based on comments received, we request the Board to consider the governance structure related to employee benefit plan audits and how it may affect the auditor's communications.

Appendices

The following includes our response to the Board's specific question related to the Appendices.

22. Is the information included in Appendices A - C to the proposed standard sufficiently clear? Should the appendices include other matters, e.g., should other items be included in an audit engagement letter?

    We have no comments on the Appendices, other than those included in response to the Board's other questions. With respect to our response to question 4, Appendix C should be modified to include the audit committee's responsibilities, as part of its oversight of the company's financial report process, to inform the auditor of matters of which the audit committee is aware that would affect the overall audit strategy, including the scope, timing, and direction of the audit, which would include matters such as:

    - Views about the risk of fraud, including identified or suspected fraud.
    - Awareness of complaints or concerns regarding accounting or auditing matters.
    - Awareness of violations of laws, regulations, or contracts.

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