From: Art Siegel [mailto:a.siegel55@gmail.com]
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To: Comments
Subject: Docket Matter No. 34

I am pleased to comment on the Board's proposal.

Introduction

I am a retired partner of Price Waterhouse LLP (PW) and served for seven years as Vice Chairman of the Firm in charge of the audit practice. During my 37-year career with PW I also served as Chairman of both the AICPA's SEC Practice Section Executive Committee and AcSec's task force on risks and uncertainties. I was also a member of FASB's EITF, FASAC and other task forces.

After retiring from PW I was appointed executive director of the Independence Standards Board and served in that capacity throughout the Board's almost four years of operation.

For the last ten years I have been a director and chairman of the audit committee of an SEC registrant and a consultant and expert witness on various accounting and auditor independence issues.

Overall Philosophy

My overriding philosophy is that management, which is in possession of the most information that is relevant to users of financial statements and related SEC filings, should continue to have the sole responsibility to report such information publicly. However, the auditor plays a crucial role in reporting on the reliability of the financial statements and that role can be usefully expanded to include other information in SEC filings, financial press releases and similar management-prepared communications.

My comments which follow are predicated on that overall philosophy.

Detailed Response

My experience as a board member has made it abundantly clear that the auditor's knowledge of a client's affairs, while significant, is only a subset of the total information available to management. Moreover, while board members may be better informed on some matters, even their knowledge in many cases represents only the tip of the iceberg. This limited knowledge is the inevitable result of the part-time or highly-focused involvement of the auditor and audit committee vs. the full-time and broad-based involvement of the management team.

In particular, while the auditor has access to the financial records of the company, minutes, and other evidential matter, and holds discussions with officers and other personnel of the company, the auditor does normally not participate in internal discussions of strategic, operational, legal and accounting issues, does not routinely deal directly with vendors, customers, lawyers, bankers and other relevant third parties, nor does the auditor have access to emails and other communications between and among company officials and outsiders.

The implication of this knowledge gap is that it is unrealistic to assume that the auditor can independently report useful and credible information beyond what is required by GAAP and that management has decided is not otherwise required. In fact I predict that if such a proposal were adopted the information reported by the auditor will, in the vast majority of cases be wrong, incomplete, misleading or at best redundant to what the company has reported. The results will be users who are burdened with unnecessary and perhaps inaccurate disclosure. More importantly, it will result in a blurring of the very important distinction between the auditor who reports on the completeness and reliability of specified management assertions and management which must decide what public disclosures are required under both GAAP and the law.

Moreover, the proposal does not recognize that substantive discussions about what should be disclosed are normally conducted by the auditor with management and when necessary with the audit committee and legal counsel. As noted in the Concept Release, the auditor is already required to be satisfied that the disclosures in SEC filings that are outside the financial statements are not inconsistent with his knowledge and with the financial statements.

The AICPA's project on risks and uncertainties was intended to have management focus on and publicly report on the uncertainties facing the company which could materially affect the financial statements. If the standard now adopted is not accomplishing that purpose, then it should be revisited and improved, rather than trying out a new and highly problematic auditor reporting model.

The proposal raises a number of related issues. For example:

- what if the auditor and management discuss the same item differently? Will the SEC allow such disparities? If not, how will they be resolved? If the SEC insists on comparability what advantage is there to the user to reading similar information? On the other hand, If differences are allowed, which disclosure should the user to believe? And what role is envisioned for the audit committee in resolving such differences and what will that mean for audit committee and board liability?

- will the auditor resort to the kinds of laundry lists of risk factors that now bulk up SEC filings but in many cases do little to inform the user of relevant risks?

- will firms develop industry-specific risk factors that are not necessarily relevant to a particular client but get reported "to be on the safe side?"

- will the fact that auditors will be issuing their own AD&A impede or encourage communication among management, audit committees and auditors? Will the role of the auditor become more adversarial, without any resulting benefits to the integrity of the financial reporting process?

Other matters:

Expanding auditor reporting responsibilities - I strongly support requiring the auditor to explicitly report on MD&A and on financial press releases and similar information. The likely additional discipline and qualitative improvements in many cases would be worth any incremental cost, especially if the reporting were only to the audit committee (which should be sufficient if it were mandatory). The Board's standard for this reporting is appropriate for these purposes.

The Concept Release asks whether the auditor's report should state that the auditor "has complied with the applicable independence requirements of the PCAOB and SEC". I think this is the wrong question. It reinforces the "rules-compliance" mindset that prevails today in the auditing profession in dealing with accounting as well as with independence issues. ISB standard 1 (now incorporated with modification in Board standards) was intended to focus the auditor on his responsibility to maintain his objectivity. The Conceptual Framework issued by the ISB in 2001 and whose underlying principles are now reflected in independence standards adopted internationally as well as by the GAO and AICPA focus on threats to independence and possible offsetting controls. No set of rules can cover all situations. For example, can a partner maintain his objectivity while auditing a close friend? A cousin? Are there different threats if it is a friend or cousin of a manager or staff accountant? Are there any offsetting controls that might be effective? Who should be informed about potential impediments to objectivity at the client? Within the firm? The audit committee? Other examples: is there a level of fees from a client in relationship to total firm, office or department that would impair objectivity? What if it is fees paid to an office doing "branch work"? Are there controls that might mitigate such threats? A threats and safeguards approach requires the auditor, and management and the audit committee, to think about the nature of the auditor's objectivity, rather then whether he is in compliance with the detailed independence rules.

The Board should undertake a comprehensive project to consider a threats and safeguards, principles-based approach to auditor independence. It is the best way to ensure that all involved understand the goal of auditor independence - objectivity -

and to provide a methodology to resolve new issues that can be understood and debated by relevant stakeholders.

Finally, I do not believe that requiring the auditor to discuss the principal auditing procedures applied to relevant items would improve the usefulness of the auditor's report. The user is not in a position to assess the relevance of those procedures, their completeness or the effectiveness with which they were applied. As stated earlier, if the requirements by the company to disclose risks and uncertainties and other material information are inadequate, those requirements should be fixed. That would retain the responsibility for disclosure with management, where it belongs.

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Please contact me if my comments require any amplification or clarification.

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