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

Re: Rulemaking Docket No. 34

Ladies and Gentlemen:

I am writing in response to your request for public comment on a variety of items covered in this Docket number related to the Auditor's Report. My comments are based on my 46 years teaching corporate and institutional finance at the graduate business school level and my involvement in the applied world—as a user rather than a generator of financial information. I have served as board member of three NYSE companies, audit committee member of each, chairing the audit committees of two, as well as a board and audit committee member of a small-cap private company.

Having reviewed some of the comments submitted on this Docket, I find myself in total agreement with Professor James L. Fuehrmeyer, Jr., of the Mendoza College of Business Administration of the University of Notre Dame, who wrote you on July 5, 2011. To avoid wasting time, therefore, I do not propose to repeat his and similar comments but rather to make a few broader points about the proposals.

First, the “many” and “some,” whose desire for further information is frequently cited as a reason for this study, appear to confuse the task of the independent external auditor with that of the securities analyst. The former's task, dealing largely with the current and the past, is to determine whether management's presentation of an entity's financial statements are fairly stated, according to established principles and practices, in all material respects as of a specified date. The latter's task is to speculate and opine on what the future of the company and its value will be. The analysts performs their task with few established principles, practices, and standards against which their output can be measured. There is little legal requirement that the analysts perform their tasks with anything like the great care demanded of the independent auditor. Furthermore, the analyst's speculation and opinions are considered free speech and thus protected from challenge except in unusual instances.

The independent auditor, of course, has to consider the future in many instances, such as in validating depreciation assumptions and percent-of-completion calculations. These are technical items, however, distantly related to the concerns of the securities analyst. To think that the independent auditor should also function as a securities analyst or could effectively serve both functions suggests a misunderstanding of one function if not both. If implemented, many of these proposals would require independent auditors to set up the equivalent of a securities analysis department. Unless somehow held to new, more rigorous standards, the resulting opinions would be worth no more than those of a securities analyst. (For example, consider the analyst who recommended a company increase its market price by increasing its yield.)

Second, the “many” who are said to want more insight from the independent auditor in the form of additional comments or highlights to management’s discussion and analysis appear to want someone else to do their research work. (The more cynical might think that the insights of the independent auditors are sought to replace the information provided hithertofore by the “expert” networks.) The pro forma example of an auditor’s comments provided in the June 9, 2011, letter from Ms. Cynthia M. Fornelli on behalf of the Center for Audit Quality, are clearly merely restatements of what already would appear in the management discussion. At best, it is a sort of executive summary, adding nothing but perhaps enabling the careless reader to skip management’s comments.

This result hardly reflects the aims and hopes of current security regulation. At worst, it is simply adding pages to documents that are already tedious to read and far too full of repetitions. The practice would also expose the independent auditor to litigation on the grounds that the auditor’s comments did not emphasize something of importance in management’s discussion that the “many,” relying on the executive summary, did not find for themselves.

Third, many aspects of the proposals would alter the dynamics of the relationships among the auditors, the audit committee, and the management. At the moment, management proposes, the auditors either disagree, agree, or raise alternatives that should be considered. In the case of public companies, a disagreement is resolved in favor of the auditors because otherwise the required filings are not possible. Agreement presents no problem. The discussion of alternatives, presumably all of which fall within accepted accounting standards, should be helpful to the audit committee and, ultimately, to management.

If the auditors were required to disclose these discussions, concern about litigation would tend to eliminate the useful communication of alternatives. The resolution would become “my way or the highway” because the independent auditor could hardly allow potential litigation about not having insisted on an alternative that the audit committee did not select. The proposal might even result in “informal” discussions in advance of any formal meeting so that a consensus in advance would be established.

And, of course, considering the number of items in a set of financial statements, even for a small company, for which alternative reasonable approaches are possible under the accepted accounting policies, the list and explanation of these for each point would make the financial reports even more cumbersome than they are at present. At the extreme, financial statements would have to be prepared showing the effect, singly and in combination, of the alternatives discussed. The “many” would appear hardly to be able to make this analysis for themselves. Without these presentations, the simple discussion would be worthless. It is hard to believe this elaboration would provide any appreciable additional insight for the “many,” who seem to seek the quick sound bite.

Third, for good reasons, the objective is that all the information the “many” request is to be provided without becoming boilerplate language. This objective seems very optimistic. The sample provided by the Center for Audit Quality runs to four solid pages of boilerplate. If I am correct that the type of information the “many” want is not the type of information an independent accounting firm is structured to provide, it is natural that the result will be boilerplate, constructed to comply in form while reducing the chance of litigation.

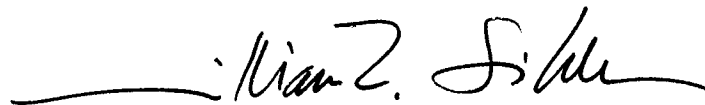
Nevertheless, it does make sense to allow the independent auditor to explain somewhat more completely in the attestation just what the independent auditor does not do and what is the responsibility of management. Thus, the addition of a few well-chosen phrases or words to the current rubric could help the uninformed investor understand that the independent auditor's role is a limited one and cannot guarantee one-hundred percent accuracy of the financial reports.

Fourth, I have a hard time imagining just what form the attestation by an independent auditor of any forward-looking statement would take. The existing boilerplate provided by management in the 10-K under SEC safe-harbor regulations indicates that statements dealing with the future are no more than best guesses as of a certain date. Securities analysts are not held to that high a standard. It appears that the "many" want a more formal certification by the independent auditor of those forward-looking comments. This requirement implies that the independent auditor would have to be at least as informed about a firm's business and its prospects as management is. One major reason for the independent auditor is that the auditor knows more about accounting principles than even the firm's financial managers, not because the independent auditor knows more about the firm's operations and prospects.

Finally, it would certainly be nice to have an independent party review the reports of management and, for that matter, of the independent auditors, if one could be found which would have better insights than the management and the independent auditors. And, of course, then a fourth party would be needed to vet the conclusions of the third party, and so on. I am reminded that not very long ago, it appeared that audit committees would have to engage their own independent auditors to review the work of the company's independent auditor. Fortunately, the idea was dropped by the wayside, apparently replaced by the PCAOB's responsibility to monitor the quality of independent auditing firms.

In conclusion, it strikes me that the "many" are trying to entice the PCAOB into doing the job of the SEC. If the "many" do not think that managements are presenting enough information or in the appropriate form, the proper body to address is the one responsible for public disclosure not the one responsible for proper accounting. Organizations tend to expand into adjacent turf when they do not have enough to do on their own field. The PCAOB certainly has many challenges in its own area. I urge the Board not to allow "many" to distract it from the excellent work it is doing where it has been given responsibility and thus to drop this study in favor of including a slightly more elaborate statement in the attestation of what the independent auditor cannot do.

Respectfully,



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