



30 September 2011

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington DC 20006-2803
USA

Email: comments@pcaobus.org

Ref.: AUD/PRJ/HBL/LAN/SHA

Dear Sir or Madam,

Re: PCAOB Rulemaking Docket Matter No. 34: Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards

FEE is pleased to provide you with its comments on the PCAOB Rulemaking Docket Matter No. 34: Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards.

The recent debate regarding auditor communication has highlighted the need to provide the public with more details of what an audit is and more information on audit performance. FEE believes that it is important to carefully consider the arguments put forward and to reflect on which lessons can be learned from the financial crisis, as the debate has shown that the way that auditors communicate is a political issue as well as a technical issue. Even if auditors have been criticised during the financial crisis for not being sufficiently sceptical, audit remains of essential value to society in today's changing economy as an independent check of the validity of the financial information provided to users in the markets. Undoubtedly, now is the right time to consider whether there is scope for enhancing the role of the audit and of the auditor to maximise their contribution to the world economy.

As the PCAOB will be aware, the IAASB is currently also discussing this topic of improvements to auditor reporting in their recently published Consultation Paper on "Enhancing the Value of Auditor Reporting: Exploring Options for Change". It would be preferable that a truly global solution for these improvements is found, to the benefits of investors and other users of financial statements and audit reports. Therefore, FEE encourages the PCAOB to closely cooperate with the IAASB when deciding on the improvements that will be introduced.

FEE has only responded to the questions in the PCAOB Concept Release that are relevant from a European or international perspective, and has not expressed views on issues that focus on purely national US matters. Our detailed responses to the relevant questions, set out below, can be summarised as follows:

1. Changes are welcome and should be introduced to improve the communicative value of audit reports by carefully considering the comments made by various stakeholders of the current audit report being too generic and containing boilerplate language. The aim should be to provide better information, instead of merely providing more information to the users.
2. The key principle is that it is the responsibility of management and those charged with governance of an entity to provide the information on an entity that is required by users. The audit report only accompanies the information provided by the audited entity itself.
3. More company specific information about the audit could be provided by the auditor, such as information on audit risks. It will be essential to clearly specify which audit risks should be disclosed. Should it be the key audit procedures that have been performed in response to the key business risks of the company or the risks of material misstatements identified by the auditor as part of the risk assessment which might not be related directly to the key business risks of the company?
4. The auditor could provide more assurance outside the current scope of audit. This should be based on a generally accepted framework and on market requests for such additional assurance.

Question 1 Many have suggested that the auditor's report, and in some cases, the auditor's role, should be expanded so that it is more relevant and useful to investors and other users of financial statements.

a. Should the Board undertake a standard-setting initiative to consider improvements to the auditor's reporting model? Why or why not?

An important role of the audit profession is to contribute to add transparency and provide comfort as to the reliability of corporate reporting. Audit and auditor communication should develop alongside corporate reporting. Auditors should also explore the opportunities to fulfill their role of providing assurance in areas such as governance, sustainability reporting, corporate governance statements, etc. which bring together financial and non-financial reporting. Since the audit is an integral part of the financial system operating in today's rapidly changing world, it is essential to consider the role of the auditor in the financial reporting system, as well as the way that auditors communicate, in a dynamic way rather than in isolation.

It should be ensured that any solutions are sought in a global context, aiming at harmonisation, and taking note of the explicit views of the users of auditor's communication. Close cooperation between the audit profession at global level and its stakeholders, including users and various regulators, is therefore needed to achieve a truly sustainable solution that will be perceived as bringing considerable added value to audit communication.

Question 2 The standard auditor's report on the financial statements contains an opinion about whether the financial statements present fairly, in all material respects, the financial condition, results of operations, and cash flows in conformity with the applicable financial reporting framework. This type of approach to the opinion is sometimes referred to as a "pass/fail model."

a. Should the auditor's report retain the pass/fail model? If so, why?

Retaining the clear "pass/fail" nature of the audit report has received great support in recent consultations, including in the European Commission Green Paper on Audit Policy. Any changes should therefore ensure that this clear message from the auditor to the users of the financial statements and the audit report remains as it is today.

Question 3 Some preparers and audit committee members have indicated that additional information about the company's financial statements should be provided by them, not the auditor. Who is most appropriate (e.g., management, the audit committee, or the auditor) to provide additional information regarding the company's financial statements to financial statement users? Provide an explanation as to why.

FEE agrees that disclosures about the entity should be provided by the company itself and not by the auditor. It is first and foremost the responsibility of the company to meet the needs of the users of financial information and they should therefore provide the relevant disclosures regarding for example critical accounting policies. The audit report only accompanies the information provided by the audited entity itself.

Auditors Discussion and Analysis - Questions 5-12

FEE believes that the auditors could be responsive to the request from users of financial statements and could therefore provide more company specific information about the audit.

Given the rapid developments in technology, providing additional information has become easier, although it may still entail additional costs to do so. FEE fully subscribes to the aim of improving the quality of the information provided to users of financial statements. Increasing the quality of the information provided rather than the quantity would be most efficient for all market participants, and would, in our view, be a more appropriate way to support investors in their decision-making process.

However, the proposed Auditors Discussion and Analysis would in our view be too extensive and risks resulting in duplication of information in already lengthy reports, as some of the information should already have been provided by the company itself, as for instance in the MD&A. FEE strongly believes that the aim should be to provide better information and not just more information.

Also, the auditor already provides this information to those charged with governance. The information needs of external users will differ from those charged with governance and it is

important to ensure the proper balance of information disclosed to the various user groups in order to facilitate their decision making process in the best way possible.

Although there could be merit in providing some of the information suggested within this model, for instance in relation to audit risks, which may or may not be related directly to the key business risks of the company, FEE believes that the model as proposed would not serve the needs of the users due to its duplication of information. Also, more attention within the model is needed to clearly distinguish between the reporting responsibilities of management and of the auditor, respectively.

Required and Expanded Use of Emphasis Paragraphs - Questions 13-18

In the recent debate, investors and other users have expressed a desire for more reporting from companies as well as from auditors. Taking note of these requests from users of financial statements and audit reports, such additional information could contribute to the important aim of reducing the current information gap between the information needs of users and the information provided by the auditors.

FEE believes that emphasis paragraphs should remain as paragraphs that are used to draw users' attention to matters that are of such importance that they are fundamental to users' understanding of the financial statements and the audit. Emphasis paragraphs should therefore remain as they are today and their application should be in situations of major importance.

Emphasis paragraphs should not be misused to compensate for the increasing complexity of financial statements. This increasing complexity is an issue that should be addressed as a matter of urgency, but this should be done by those responsible for the financial reporting framework and by preparers so that readable and understandable financial information is provided to stakeholders. This problem can not and should not be solved by the auditing standard setter through imposing additional reporting responsibilities on auditors.

The French requirement of "*justification of opinion*" is one example of how to approach the reduction of the information gap. The current French requirement states that the justification must "... enable the user of the report to obtain a better understanding of the reasons behind the statutory auditor's opinion on the financial statements".

This principle appears appropriate and could be further explored. In doing so, comments and suggestions for improvement due to the diversified and inconsistent application seen in French audit reports should be carefully considered in order to avoid generic boilerplate language and to ensure that the request from users of providing more decision-useful company-specific information related to the specific audited company in question is de facto met.

It should be made sufficiently clear that this additional "*justification of opinion*" acts in conjunction with the pass/fail nature of the opinion as well as with qualifications and emphasis paragraphs in the audit reports. To avoid any confusion between "justification of opinion" paragraphs and "Emphasis" paragraphs, a term such as "Expanded emphasis paragraphs" should be avoided.

Auditors Assurance on Other Information Outside the Financial Statements - Questions 19-20

The areas suggested are in relation to non-GAAP information, which could be in relation to, for example, corporate governance arrangements, the sustainability of the business model and key performance indicators.

FEE believes that the company could extend their reporting on such matters. The auditor could then provide additional assurance provided that there is a general request from the market to deliver such assurance services. The information may not necessarily be included in the financial statements, but could be provided outside the financial statements. The assurance given by the auditor on these matters should be separated accordingly.

The level of involvement could vary from no involvement to the auditor providing assurance on the entire content of the annual report and should depend on what users require. Further debate with all relevant stakeholders on proposals for additional management reporting on these matters would be needed to balance the information needs of the investor community. The additional disclosed business information should also not be detrimental to the commercial interests of the company. It is important that the assurance services are developed in response to these market requests for additional information.

Clarification of the Standard Auditor's Report - Questions 21-22

The audit report is the core deliverable from the auditor. In order to preserve this core service, the comments on the usefulness of the audit report and suggestions for improvements from the users should be carefully considered. Changes made should be sustainable to allow for continuous changes to reporting and society in general.

FEE believes that the criticism of the current audit report being too long and defensive with too much boilerplate information is valid and there is clearly merit for rethinking the format and the structure of it. This could be done by reducing the technical jargon to a minimum with the aim of making it as understandable as possible for the reader.

Reducing this generic information in the audit report will also underline that an audit is not a generic product, but is a service that, although based on the same principles, is tailored to each specific audited entity. It will underline that the audit report is the result of a process conducted by the auditor that is based on the knowledge and experience of the auditor of that particular audited entity.

Question 23 This concept release presents several alternatives intended to improve auditor communication to the users of financial statements through the auditor's reporting model. Which alternative is most appropriate and why?

Comments made by various preparer and user groups in other consultations¹ indicate that the changes that appear to be most responsive to the comments made on the current audit report appears to be related to the format and structure of the audit report itself. This could be done by reducing the amount of generic information in the audit report, also by communicating through using less audit technical language.

Retaining the clear “pass/fail” nature of the audit report has received great support. Any changes should therefore ensure that this clear message from the auditor to the users of the financial statements and the audit report remains as it is today.

The focus should be on reducing the “information gap” rather than the “expectation gap”. Without disregarding the expectation gap, there may be greater value in such a prioritisation, as the expectation gap will most likely continue to exist. Instead, the clear aim should be to enhance the value of audit through better, instead of more, communication. Changes regarding the audit report would most likely have the greatest impact on the perception of the value of audit, if they focus on matters related to format and structure.

Question 24 Would a combination of the alternatives, or certain elements of the alternatives, be more effective in improving auditor communication than any one of the alternatives alone? What are those combinations of alternatives or elements?

It should be carefully considered whether and how the changes explored in the Concept Release operate in conjunction with each other. For instance, an AD&A in a more limited format than proposed in the Concept Release and increased use of Emphasis paragraphs or combined with introducing “justification of opinion” as in France may result in duplication of requirements and of information disclosed.

Question 29 What effect would the various alternatives have on audit quality? What is the basis for your view?

It is essential that any initiatives to improve auditor reporting do not impact or impair audit quality, as any changes should only be introduced if they add value for the users of financial statements. Although it may not be possible to serve all user needs, the aim should be that the majority of users perceive the changes to be an improvement and that their information needs are better served.

¹ See the outcome of the consultation in the EC Green Paper on Audit Policy and the summary of responses on the IOSCO Consultation Paper on Auditor Communication, both in 2010.

For further information on this FEE² letter, please contact Hilde Blomme at +32 2 285 40 77 or via email at hilde.blomme@fee.be or Lotte Andersen at +32 2 285 40 80 or via email at lotte.andersen@fee.be from the FEE Secretariat.

Yours sincerely,



Philip Johnson
FEE President

² FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 45 professional institutes of accountants and auditors from 33 European countries, including all of the 27 European Union (EU) Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 500.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

FEE's objectives are:

- To promote and advance the interests of the European accountancy profession in the broadest sense recognising the public interest in the work of the profession;
- To work towards the enhancement, harmonisation and liberalisation of the practice and regulation of accountancy, statutory audit and financial reporting in Europe in both the public and private sector, taking account of developments at a worldwide level and, where necessary, promoting and defending specific European interests;
- To promote co-operation among the professional accountancy bodies in Europe in relation to issues of common interest in both the public and private sector;
- To identify developments that may have an impact on the practice of accountancy, statutory audit and financial reporting at an early stage, to advise Member Bodies of such developments and, in conjunction with Member Bodies, to seek to influence the outcome;
- To be the sole representative and consultative organisation of the European accountancy profession in relation to the EU institutions;
- To represent the European accountancy profession at the international level.

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