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

28 May 2013

**Proposed Framework for Reorganization of PCAOB Auditing Standards and Related Amendments to PCAOB Auditing Standards and Rules, PCAOB Rulemaking Docket Matter No. 40**

Dear Office of the Secretary:

Ernst & Young LLP is pleased to submit comments on the request for comment from the Public Company Accounting Oversight Board (PCAOB or the Board) on its proposed framework for reorganization of PCAOB auditing standards and related amendments (the proposed reorganization).

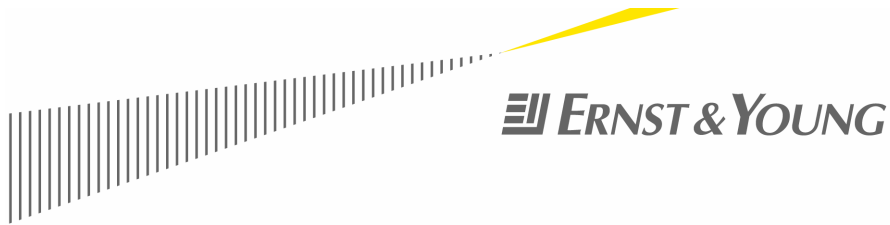
We agree that the Board's existing auditing standards, consisting of sequentially numbered standards issued by the Board (the AS standards) and the AU sections representing the remaining interim standards that the Board has not superseded, present a confusing framework. While we agree that reorganization is needed and may help users navigate the standards more easily, we do not agree with the Board's assertion that the proposed reorganization would help avoid confusion between the Board's standards and the recently reorganized standards of the ASB<sup>1</sup> or that the reorganized structure could facilitate comparison of PCAOB and IAASB standards.<sup>2</sup>

In order to enhance audit quality, we believe a better solution would be to have one common framework for auditing standards that clearly demonstrates the performance differences for audits of issuers and non-issuers. Therefore, we recommend that the Board collaborate with the IAASB and the AICPA on a longer-term project to develop a unified framework for all audit standard-setters that would become a base from which the standard-setter could then customize its individual standards. This approach would clearly present the performance differences between the standards. In addition, with all of the truly important matters on the Board's standard-setting agenda right now, we question whether it makes sense for the Board to pursue the proposed reorganization in 2013.

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<sup>1</sup> Section I. Introduction, paragraph 5 of PCAOB Release No. 2013-002.

<sup>2</sup> Section II A. Proposed Framework for Reorganization of PCAOB Auditing Standards, paragraph 5 of PCAOB Release No. 2013-002.



We therefore do not support the proposed reorganization at this time. In the remainder of this letter we more fully explain our concerns and suggested alternative, which we have organized in the following areas:

- ▶ Need for unified auditing standards framework
- ▶ Timing and costs of proposed reorganization

In addition, we have provided overall comments on the proposed reorganization, as well as detailed comments for your consideration, in the event the Board decides to move forward with the proposed approach.

We would be pleased to discuss our comments with members of the PCAOB or its staff.

Sincerely,

*Ernst & Young LLP*

### **Need for unified auditing standards framework**

We recognize that the Board considered the option of adopting the organizational structure of another standard setter, such as the IAASB, and decided that there are a number of potential drawbacks that could make that approach less desirable than the proposed reorganization.<sup>3</sup> However, we believe that significant benefits can be obtained, while maintaining the integrity of the intentional differences in the PCAOB standards, by collaborating with other standard setters to create a common framework to represent the base for auditing standards. We believe the most important aspect of starting with a common framework would be increased transparency. That is, the incremental performance differences for audits conducted under PCAOB auditing standards and those conducted under AICPA or IAASB auditing standards would be clear.

We believe the proposed reorganization, which diverges from the framework of the AICPA and IAASB, may impede an auditors' ability to understand these differences. As the PCAOB continues to adopt new standards, we can envision that auditing standards will diverge to a greater extent. As the differences in the requirements and performance expectations become less apparent, auditors would be less likely to execute audits in accordance with the applicable US auditing standards because it would be harder for them to understand the differences in the performance expectations of the varying standards.

We appreciate that Appendix 3 to the release accompanying the proposed reorganization compares the proposed reorganization of the PCAOB auditing standards to the standards of the IAASB and ASB; however, we don't believe this comparison addresses the bigger issuer that auditors have to face when navigating the auditing standards. Many auditors audit both issuer and non-issuer entities. Having essentially the same standards identified differently by the two standard-setting bodies, with some expected performance differences that are not clearly articulated, would cause confusion. It would also increase costs because firms would attempt to interpret and address the different standards in their guidance and training materials. To promote the execution of high-quality audits, we believe the Board should collaborate with the other standard setters to develop a framework as a baseline and allow auditors to better understand the differences between the various sets of auditing standards that they are required to apply.

### **Timing and costs of proposed reorganization**

The Board currently has an ambitious standard-setting agenda focusing on the truly important matters facing auditors today (e.g., auditing estimates and fair value measurements, the auditor's reporting model, quality control standards). We support the Board's effort to align its standard setting with what the Board is seeing in inspections and hearing from stakeholders. We don't believe that the proposed project fully responds to either of these inputs. In addition, we don't believe that the benefits of the proposed reorganization, which include only reordering and renumbering existing standards without making substantive changes to the requirements of the standards, are necessary at this time or would provide benefits that would outweigh the cost to practitioners. The costs incurred as a result of the proposed reorganization would be significant, and would include updates to firms' methodology, guidance, enablers, technology tools and training materials to reference the new standards organization, both in and outside the US.

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<sup>3</sup> II.B Consideration of Alternatives, paragraph 5, of PCAOB Release No. 2013-002.

We believe the PCAOB should look at this as a longer-term, collaborative project with the other standard setters that will result in a framework that will add benefits to practitioners and increase audit quality.

### **Overall comments on proposed reorganization**

If, after considering comments on the proposed reorganization, the Board decides to pursue the project at this time, we offer the following overall comments on the proposed reorganization.

#### ***Overall reorganization***

We agree that organizing the PCAOB's auditing standards into a topical structure with a uniform numbering system is an improvement to the current numbering system. We also agree with reordering and renumbering the existing standards in their entirety, without redrafting the auditing standards or making substantive changes to the requirements of the standards. Finally, we agree with the Board's effort to rescind certain auditing standards that it believes are no longer necessary as part of the proposed reorganization.

However, we are concerned that combining the PCAOB's interim auditing standards, many of which have not yet been updated by the Board, with the standards issued by the Board, will make it difficult for auditors to readily identify standards that the PCAOB has not yet analyzed and updated. Currently, we can easily identify the interim standards, and therefore, more easily interpret the standards as necessary, with the knowledge that they have not yet been updated to apply specifically to issuer audits. Therefore, we suggest that the Board consider including an indicator in the proposed reorganization that will identify sections that have not yet been updated by the Board.

While the proposed reorganization generally follows the flow of the audit process, we have some suggestions about the naming, numbering or placement of certain categories and subcategories that we believe would improve the proposed organization of the PCAOB's auditing standards (see Detailed comments below).

#### ***AU Section 532, Restricting the use of an auditor's report***

We support the PCAOB's proposal to eliminate references to generally accepted auditing standards or outdated references to accounting standards. However, we believe that PCAOB AU section 532, *Restricting the Use of an Auditor's Report* (PCAOB AU 532), should not be rescinded. PCAOB AU 532 addresses restricting the auditor's report and we believe it is important that PCAOB auditing standards provide the opportunity for an auditor to restrict the use of the auditor's report (and, more broadly, other written communications), when appropriate. As the Board stated in the release accompanying the proposed reorganization, it is not the intent of the PCAOB to substantively change practice as a result of the final implementation of the proposed reorganization; however, we believe the proposed PCAOB AU 532 rescission would cause a substantial change in practice. If the standard is rescinded, auditors also may think the PCAOB's standards no longer permit auditors to restrict the use of other written communications.

Finally, we observe that guidance associated with restricting the use of an auditor's written report in PCAOB AU 532 is referenced in other PCAOB standards, such as Auditing Standard No. 16, *Communications with Audit Committees* (AS 16).

## ***AICPA auditing and accounting guides***

We acknowledge the appropriateness of the PCAOB standards no longer requiring auditors to “be aware of and consider” the AICPA Audit and Accounting Guides in existence on 16 April 2003 because these publications may be outdated. However, we believe that auditors, particularly in specialized industries, need supplementary guidance in applying auditing standards to the unique aspects of those industries, particularly when specific PCAOB auditing guidance does not exist (e.g., related to the audits of airlines, gaming issuers, issuers with oil and gas producing activities). Recognizing that the PCAOB does not have the development and maintenance of specialized industry guidance on its current standard-setting agenda, it would be helpful for the proposed reorganization to acknowledge that auditors may use the current versions of the AICPA Audit and Accounting Guides, while taking into consideration the differences between AICPA and PCAOB standards.

### **Detailed comments**

We suggest the following potential changes to the naming, numbering or placement of certain categories and subcategories of the proposed reorganization (Appendix 1 – Proposed Framework for Reorganization of PCAOB Auditing Standards):

- ▶ Under the bold heading, **General Auditing Standards**, we don't believe there is a sufficient differentiation between the subtopics *1100 General Concepts* and *1200 General Activities*. Therefore, we suggest that these two subtopics be combined into one subtopic (e.g., *General Concepts and Activities*). We also suggest that the *Auditor Communications* subheading be elevated to a main, bolded heading.
- ▶ We suggest that the Board change the name of the subheading *2200 Audit Procedures in Response to Risks – Nature, Timing, and Extent*. While this section describes procedures the auditor performs in response to identified risks, we believe there are other audit procedures that the auditor performs to respond to risks (e.g., *2501 Auditing Accounting Estimates, 2502 Auditing Derivative Instruments, Hedging Activities, and Investments in Securities, 2502 Inventories*) that are not included under the 2200 series. We believe the subheading 2200, as proposed, implies that only the procedures under the 2200 series are designed to respond to risk, which is not accurate.
- ▶ We suggest moving *2302 Reporting on Whether a Previously Reported Material Weakness Continues to Exist* to the section titled **Other Matters Associated with Audits** because we don't believe this topic is directly related to audits of financial statements.
- ▶ We suggest moving *2602 The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements* to the 1200 section of the framework. We believe this topic should be treated similarly to *1202 Part of Audit Performed by Other Independent Auditors and 1203 Using the Work of a Specialist*.
- ▶ The Board is proposing to change the name of AU sec. 558, *Required Supplementary Information*, to *2702 Unaudited Supplementary Information Included in Audited Financial Statements*. We note that the AICPA clarified standard (AU-C 730, *Required Supplementary Information*) addressing the same topic has retained the title *Required Supplementary Information*. In order to retain similarities in the name of AU sections that address the same subject matter, and thus reduce auditor confusion, we suggest that the Board retain the name *2702 Required Supplementary Information*.

- ▶ We believe that proposed subcategories *2701 Reporting on Information Accompanying the Basic Financial Statements in Auditor-Submitted Documents* and *2702 Unaudited Supplementary Information Included in Audited Financial Statements* should be placed under subcategory *3300 Other Reporting Topics*. We note that these subcategories address standards for auditor reporting, rather than standards for planning and performing audit procedures or gathering audit evidence.
- ▶ We suggest that the Board move *2805 Evaluating Consistency of Financial Statements* to the **Auditor Reporting** section of the proposed framework.
- ▶ While we note that *3310 Special Reports* contains some guidance applicable to issuer audits, it also contains guidance that would not be applicable to issuer audits (guidance related to financial statements prepared in conformity with a comprehensive basis of accounting other than generally accepted accounting principles). While we understand that the Board does not want to make substantive changes to existing standards, we believe it would be confusing to auditors to see guidance that is clearly not applicable to issuer audits included in the revised PCAOB auditing standards framework.
- ▶ *6103 Compliance Auditing Considerations in Audits of Recipients of Governmental Financial Assistance* (extant PCAOB sec. 801) is applicable when the auditor is engaged to audit a governmental entity under generally accepted auditing standards (GAAS), and engaged to test and report on compliance with laws and regulations under Government Auditing Standards (the Yellow Book) or in certain other circumstances involving governmental financial assistance, such as single or organization-wide audits or program-specific audits under certain federal or state audit regulations. Since the terms and conditions of the governmental financial assistance requires that these engagements be performed under the Yellow Book, and therefore also in accordance with generally accepted auditing standards, we are not aware of circumstances when this section would apply to auditors performing audits under PCAOB standards. Therefore, we suggest that the Board rescind this section from its auditing standards.