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Phoebe W. Brown, Secretary
Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

30 August 2017

**Re: Proposed Auditing Standard on Auditing Accounting Estimates, Including Fair Value Measurements, and Related Amendments to Certain PCAOB Auditing Standards, PCAOB Rulemaking Docket Matter No. 043**

Dear Ms. Brown:

Ernst & Young LLP (EY) is pleased to submit these comments to the Public Company Accounting Oversight Board (PCAOB or Board) on proposed auditing standard, *Auditing Accounting Estimates, Including Fair Value Measurements*, and related amendments to other standards (collectively, the Proposal). We support the PCAOB's efforts to strengthen the requirements for auditing accounting estimates, and we believe many of the proposed changes would improve the quality of auditing in this area.

We also appreciate that the Board is monitoring developments related to the International Auditing and Assurance Standards Board (IAASB) exposure draft of Proposed International Standard on Auditing 540 (Revised), *Auditing Accounting Estimates and Related Disclosures* (ED-540). We encourage the Board to work with the IAASB to develop a single approach to auditing estimates or at least minimize the differences between any final standards. We believe audit quality would be promoted with a single framework to audit estimates.

Our comments below focus on the following areas where we believe the Proposal could be improved or made more practical:

- Proposed Auditing Standard (AS) 2501, *Auditing Accounting Estimates, Including Fair Value Measurements*
- Proposed Appendix A to Proposed AS 2501, *Special Topics* (Proposed Appendix A to AS 2501)
- Proposed Appendix A to AS 1105, *Audit Evidence,* Audit Evidence Regarding Valuation of Investments Based on Investee Financial Condition or Operating Results (Proposed Appendix A to AS 1105)
- Other matters

In each section of this letter we highlight our key areas of concern and propose alternatives. The appendix to this letter contains our other observations.

**Proposed AS 2501: Auditing Accounting Estimates, Including Fair Value Measurements**

## Considerations relating to management bias

Paragraph .03 of the Proposal would require the auditor to obtain sufficient appropriate audit evidence to determine whether accounting estimates "are free from bias that results in material misstatement." We recognize the Board's intent to further emphasize the importance of the consideration of management bias in the estimates standard and go beyond the requirements in AS 2401, *Consideration of Fraud in a Financial Statement Audit*, and AS 2810, *Evaluating Audit Results*.

We believe that the auditor's objective when auditing accounting estimates should be to obtain sufficient appropriate audit evidence to provide reasonable assurance that the estimate is reasonably stated and free from a material misstatement and has been accounted for and disclosed in conformity with the applicable financial reporting framework. In our view, AS 2401, AS 2810 and the requirements included in the Proposal adequately set forth the requirements for the auditor's assessment and response to the risk of management bias in accounting estimates.

We are concerned that including bias as an explicit objective in any final standard could imply that the auditor is required to point to specific evidence to support the conclusion that the objective was met. In our view, management bias is an important consideration for the auditor when performing his or her risk assessment and in executing procedures to evaluate whether the estimate is reasonably stated and free of material misstatement. Management bias is a key input to the design and performance of the auditor's procedures, but in and of itself should not be a specific objective. We believe the Board should remove the reference to bias in the objective.

## Developing an independent expectation

Proposed paragraph .25 states that "if the auditor's independent expectation consists of a range rather than a point estimate, the auditor should determine that the range is appropriate for identifying a misstatement of the accounting estimate and supported by sufficient appropriate audit evidence." We agree with the Board that it is important for the auditor to focus on determining that a range of estimates is supported by sufficient appropriate audit evidence. However, it is not clear to us how auditors would "determine that the range is appropriate for identifying a misstatement of the accounting estimate."

We believe the Board should clarify its intent on this point. For example, we do not believe it would be appropriate that this phrase imply that a range of reasonable estimates cannot exceed the auditor's materiality threshold. This situation is not uncommon, particularly when the estimation uncertainty is high, and in some cases the range of acceptable outcomes may significantly exceed the auditor's materiality threshold. We recommend that the Board clarify the phrase "appropriate for identifying a misstatement" and state that a range could be greater than the auditor's materiality threshold, assuming that the range only includes amounts supported by sufficient appropriate audit evidence.[1]

**Significant assumptions**

We recommend eliminating the note to proposed paragraph .15, which states "if the company has identified significant assumptions used in an accounting estimate, the auditor's identification of significant assumptions should also include those assumptions." We are not aware of any requirements for management to designate assumptions as significant. Instead, management typically has controls in place to review all relevant assumptions.

Because "significant assumption" is not defined for management, we believe this requirement could create unnecessary confusion. For example, it could increase the number of assumptions that the auditor must identify as significant, even if it does not agree with management's assessment, resulting in the performance of unnecessary audit procedures in areas of lower risk. If auditors are able to demonstrate that an assumption is not significant (based on the factors provided in paragraph .15), we believe they should not be required to identify the assumption as significant solely because management did.

In addition, proposed paragraph .18 would require, for critical accounting estimates, the auditor to "obtain an understanding of how management analyzed the sensitivity of its significant assumptions to change, based on other reasonably likely outcomes that would have a material effect." We believe it would be more appropriate to align the requirement more closely with the auditor's risk assessment (e.g., by requiring the auditor to obtain this understanding for estimates affected by significant estimation uncertainty).

**Evaluating the company's methods**

Proposed paragraph .10 would require auditors to evaluate whether the methods used by the company to develop the accounting estimates are appropriate for "the business, industry and environment in which the company operates." We don't believe the PCAOB should require a separate evaluation of these factors. Instead, we believe the auditor should consider these factors when evaluating the appropriateness of the company's method. We believe the proposed requirement, as written, could lead auditors to expect that all companies in an industry should use the same methods of estimation. Therefore, we recommend the following edit to proposed paragraph .10:

> .10 The auditor should evaluate whether the methods used by the company to develop accounting estimates are:
>
> a. In conformity with the requirements of the applicable financial reporting framework; and

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[1] We also observe that the IAASB includes the following guidance in paragraphs 20 and A134 of ED-540, which we support:

20. If the auditor concludes that it is appropriate to develop an auditor's range, the auditor shall only include in that range amounts that (a) are supported by the audit evidence; and (b) the auditor has evaluated to be reasonable in the context of the measurement objectives and other requirements of the applicable financial reporting framework.

A134. In certain circumstances, the auditor's range for an accounting estimate may be multiples of materiality for the financial statements as a whole, particularly when materiality is based on operating results (for example, pre-tax income) and this measure is relatively small in relation to assets or other balance sheet measures. In these circumstances, the auditor's evaluation of the reasonableness of the disclosures about estimation uncertainty becomes increasingly important. Considerations such as those included in paragraphs A133, A144 and A145 may also be appropriate in these circumstances.

b. Appropriate for the nature of the related account or disclosure, considering ~~and~~ the business, industry, and environment in which the company operates.

**Considerations when more than one substantive approach is used**

The Proposal describes the procedures an auditor should perform to test an accounting estimate under each of the three approaches identified in proposed paragraph .07. However, it does not explain how auditors would adjust their procedures when using a combination of the approaches, which is common in practice.

For example, the auditor may use its independent estimate in combination with evidence provided by testing the company's process. While the Proposal recognizes that the auditor may use any of the three approaches individually or in combination, we believe it could better describe (1) the expectations for the auditor's performance when the methods are used in combination and (2) considerations for the auditor's evaluation of evidence.

**Auditor's responsibilities**

Guidance in AS 2502, *Auditing Fair Value Measurements and Disclosures*, states "The auditor is not responsible for predicting future conditions, transactions, or events that, had they been known at the time of the audit, may have had a significant effect on management's actions or management's assumptions underlying the fair value measurements and disclosures." We believe inherent uncertainty associated with the determination of amounts and disclosures related to estimates is an important concept that should be recognized in the PCAOB's auditing standards. We recommend this guidance be retained in any final standard and that it apply to all accounting estimates, including fair value measurements.

## Proposed Appendix A to Proposed AS 2501 — Special Topics

We appreciate the Board's efforts to address the unique audit considerations related to pricing information from third parties, and we support the development of the special topics appendix to Proposed AS 2501. However, we have concerns about the proposed requirements regarding the auditor's ability to understand and evaluate the methods and inputs used by pricing services at a group level (e.g., by asset class), as well as the conditions that must be met in order to obtain less information about the particular methods and inputs used by a pricing service when pricing information is obtained from multiple pricing services. We believe that the proposed requirements could cause auditors to perform significantly more work when auditing lower-risk financial instruments, which could result in an increase in costs for auditors, companies and pricing services, without a commensurate benefit to audit quality.

**Understanding and evaluating the methods and inputs used by pricing services at an aggregated level**

While the proposing release states that the Proposal would not require audit procedures to be applied to each individual financial instrument, we are concerned that the proposed appendix would not allow auditors to stratify financial instruments into groups for purposes of understanding and evaluating a pricing service's valuation methodologies and inputs. The proposal appears to contemplate this in proposed paragraph .A8, which indicates that if pricing information is obtained from multiple pricing services and certain other conditions are met, "less information is needed about the particular methods and inputs used by the individual pricing service."

Our interpretation of this statement is that if all conditions described in this paragraph are met, the evaluation of methods and inputs at a group level would represent a sufficient level of information about the methods and inputs used by the individual pricing service. However, this is not clear based on the wording in proposed paragraph .A8. If our interpretation is correct, we believe the Board should clarify its intent to more clearly state that "less information" would enable evaluations to be performed at a group level.

**Criteria regarding the use of pricing information from multiple pricing services**

While we agree with the principle that less information is needed about methods and inputs when pricing information is obtained from multiple pricing services, we are concerned about the extent of procedures that could be necessary for the auditor to satisfy each of the four conditions in proposed paragraph .A8.

For example, conditions .A8c and .A8d could be interpreted as requirements for the auditor to obtain an understanding of the methods and inputs for determining fair value for each financial instrument selected for testing. As described above, this procedure is often performed at a group level rather than for each financial instrument. In addition, specific information regarding valuation models and inputs may not be available to auditors from the pricing service due to its proprietary nature.

As an alternative, we believe the auditor should be able to develop an expectation about whether fair value estimates provided by multiple pricing services should be reasonably consistent. This expectation would be based on the auditor's risk assessment of financial instruments, considering the auditor's understanding of the nature and characteristics of the financial instruments, knowledge of market activity and expectations about the degree of consistency in views among market participants regarding the inputs used for determining fair value.

Proposed paragraph .A8a implies that auditors would need to obtain evidence of recent trades. While we agree that the auditor needs to understand how recent trades have been considered in the pricing service's determination, we believe this assessment can be made at the group level based on the existence of trading information for the various types of securities and other pricing information. As a result, we believe how recent trades are considered by the pricing service should be a factor for the auditor to consider in developing an expectation about the consistency of views among market participants regarding the inputs used to determine fair value.

With respect to proposed paragraph .A8b, it may be impracticable for the auditor to obtain evidence about whether the financial instruments are routinely priced by several pricing services for each financial instrument selected for testing. We believe auditors should be required to obtain this evidence at the group level, particularly since lower-risk financial instruments are more likely to be subject to the guidance in proposed paragraph .A8. Furthermore, the remainder of proposed paragraph .A8 refers to multiple pricing services, whereas proposed paragraph .A8b refers to several pricing services. We recommend that any final standard use consistent language.

Proposed paragraph .A8c would require auditors to understand the methods used to price a particular financial instrument in order to obtain less information about the particular methods. When the auditor obtains an understanding of valuation methodologies at a group level as described above, particularly for lower-risk financial instruments that would likely be subject to the guidance in proposed paragraph .A8, we do not believe it would be necessary for the auditor to understand the methods used for an individual financial instrument selected for testing pursuant to this paragraph.

Proposed paragraph .A8d could require auditors to obtain evidence about whether the valuations of all financial instruments selected for testing are generally based on observable inputs. We believe the Board should clarify that auditors could perform this assessment at a group level.

Taking a step back, in our view, the auditor should not be required to understand and evaluate the methods or inputs of the particular financial instrument being tested if all four of the following conditions are met: (1) the auditor is able to develop an expectation that fair value estimates provided by multiple pricing services should be reasonably consistent, (2) the auditor obtains prices from multiple pricing services that routinely price that type of financial instrument, (3) the prices are reasonably consistent and (4) the pricing information for the type of financial instrument is generally based on inputs that are observable.

If these conditions are met, we believe it would be sufficient for auditors to evaluate a pricing service's methodologies at a group level rather than evaluate each financial instrument. We believe that the audit evidence obtained from these procedures would be sufficient and appropriate. Based on our views, we offer the following suggestions to paragraph .A8:

> .A8 When pricing information is obtained from multiple pricing services, less information[2] is needed about the particular methods and inputs used by the individual pricing services when the following conditions are met:
>
> a. The auditor's understanding of the nature and characteristics of the particular financial instrument, including his or her expectation about whether market participants share consistent views regarding how recent trades are considered and the inputs used for determining fair value, is sufficient to develop an expectation that fair value estimates provided by multiple pricing services should be reasonably consistent; ~~There are recent trades of the financial instrument or of financial instruments substantially similar to the financial instrument being tested;~~
>
> b. The ~~particular~~ type of financial instrument is routinely priced by ~~several~~ multiple pricing services;
>
> c. Prices obtained from multiple pricing services are reasonably consistent, taking into account the nature and characteristics of the financial instrument~~, the methods used,~~ and market conditions; and
>
> d. The pricing information for the type of financial instrument is generally based on inputs that are observable.

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[2] Also refer to our comment above regarding the clarification needed with respect to what would constitute a sufficient level of information and the auditor's ability to evaluate a pricing service's methodologies at a group level.

**Proposed Appendix A to AS 1105, *Audit Evidence* — Audit Evidence Regarding Valuation of Investments Based on Investee Financial Condition or Operating Results**

We have several concerns regarding this proposed appendix, and we recommend that the Board replace it with the requirements currently included in paragraphs .28 through .34 of AS 2503, *Auditing Derivative Instruments, Hedging Activities, and Investments in Securities*.

It is not clear to us why the Board believes it is necessary to expand the current requirements. We believe that the proposed requirements would represent a significant change in current practice and would significantly increase costs for auditors, companies and their investees, without a corresponding benefit to audit quality. Our concerns are described in the following sections.

**Obtaining information from the investee's auditor**

Proposed paragraph .A4b indicates that if the investee's audited financial statements are significant to the valuation of the company's investment, the auditor should "obtain information about the procedures the investee's auditor performed and the results thereof or review the audit documentation of the investee's auditor." We believe this proposed requirement is unclear and may be difficult to apply.

For example, it is not clear to us what information the auditor should obtain, what type of audit documentation the auditor should review, and whether the auditor would be expected to apply AS 1205, *Part of the Audit Performed by Other Independent Auditors*. Furthermore, obtaining this information may not always be practicable, particularly for investees that are not controlled by the entity being audited and for investees located in foreign jurisdictions (e.g., due to privacy laws).

We note that footnote 14 in AS 2503 currently describes this as a consideration rather than an explicit requirement. There are several considerations that auditors take into account in practice to determine whether this procedure is necessary, such as the materiality of the investment to the company's financial statements and whether the investee is controlled by the entity being audited.

We believe that if the financial statements of the investee have been audited by an auditor whose report is satisfactory, auditors should be able to assess the reputation and qualifications of the investee's auditor to support the use of the investee's audited financial statements, without needing to perform the additional procedures in proposed paragraph .A4b. Any additional procedures should be based on the auditor's judgment considering the risk of material misstatement. As such, we believe the current guidance in footnote 14 to AS 2503 should be retained to give the auditor the flexibility to determine whether this procedure is necessary.

**Investment company considerations**

The note to proposed paragraph .A4 appears to provide an exception to the proposed requirement in .A4b to obtain information about the procedures the investee's auditor performed for audits of investment companies, but only if the auditor tests the "investment company's procedures for understanding the characteristics of underlying investments of the investee fund and assessing the investee fund's valuation process." It is not clear to us what it means to "test the investment company's procedures for understanding" and how auditors would perform these tests.

Also, it is not clear to us why the exception would only be provided if the auditor tests the investment company's procedures and not if the auditor independently understands the characteristics of the underlying investments of the investee fund and assesses the investee fund's valuation process, for example. Furthermore, it is not clear to us whether this exception would be limited to funds of funds based on the example provided in footnote 4 to this proposed appendix or whether the exception would apply to all investment companies as defined under the Investment Company Act of 1940, including business development companies and mutual funds. It is also not clear to us why the exception would only be provided for investment companies. We believe a company that isn't an investment company that holds an investment in a fund that was estimated using the net asset value (NAV) per share practical expedient in Accounting Standards Codification 820, *Fair Value Measurement* (ASC 820) should also qualify for the exception. We recommend that the Board clarify the scope of the exception.

**Subsequent event inquiries of investee management**

Proposed paragraph .A3b states the auditor should "make inquiries of the investee to identify subsequent events and transactions that could be material to the company's financial statements." We believe current requirements for auditing subsequent events (e.g., inquiries of management, subsequent cash testing) should be sufficient in substantially all circumstances to address this risk. Paragraph .33 of AS 2503 currently requires auditors to make appropriate inquiries of the investor to identify subsequent events and transactions that are material to the investor's financial statements. As a result, we believe the current guidance in paragraph .33 of AS 2503 should be retained.

**Practicability of the proposed requirements**

For many noncontrolling investments, investor management may not have direct access to investee management to easily arrange for the investor's auditor to perform the procedures in proposed paragraphs .A3b and .A4b, and in some cases, the investor may not be entitled to such information pursuant to the terms of the investment arrangement. In addition, for certain investees that are located in foreign jurisdictions, the investor's auditor may not be permitted to perform the proposed procedures due to foreign laws and regulations around data privacy and licensing.

As a result, the Proposal may have unintended consequences, including that the auditor could have a scope limitation on his or her ability to form an opinion when the procedures in paragraphs .A3b and .A4b cannot be performed. Alternatively, we believe the auditor could obtain sufficient and appropriate evidence by performing other procedures to test the value of the company's investment, based on the identified risks of material misstatement. We believe that if the Board decides to proceed with these or similar requirements, it needs to consider whether the investor controls the investee and the applicable laws and regulations in the circumstances, and provide guidance related to the expected auditor's response.

**Investee financial statements under PCAOB standards**

Proposed paragraph .A2d states that the auditor should read available financial statements of the investee to obtain an understanding of "whether the report of the investee's auditor indicates that audit was performed under PCAOB standards." It's unclear to us why the PCAOB is making this distinction and whether its intent is to require an auditor to consider the difference in risk between an audit conducted under PCAOB auditing standards and one performed, for example, under AICPA auditing standards. We believe the auditor's assessment of the qualifications and competence of the investee's auditor, as well as a consideration of the basis of accounting, would be most relevant to the auditor's consideration of the audited financial statements.

### Scope exclusions

Footnote 1 to the proposed appendix scopes out equity method investments when (1) the investee is audited by an auditor other than the principal auditor and (2) the other auditor is supervised under AS 1201, *Supervision of the Audit Engagement,* or the work of the other auditor is used pursuant to AS 1205. We believe the Board also should exclude from this requirement:

- Investments in entities that have a readily determinable fair value that is based on the entities' financial condition, such as mutual funds that are valued based on their NAV per share

- Investments in entities that are considered components under AS 1201 (e.g., equity method investees that are components) and audited by a component audit team that is part of the same firm as the principal auditor and supervised by the primary team pursuant to AS 1201

## Other matters

### Applicability

We believe a final standard should be applicable to all audits conducted under PCAOB standards, including audits of emerging growth companies and brokers and dealers.

### Outreach to preparers

We believe that the implementation of the Proposal, particularly the areas relating to investee financial information and pricing services, could also have implications for preparers. We encourage the Board to seek feedback from preparers on how they believe potential changes in the auditing standards could affect their processes (if at all) and consider that input before finalizing the Proposal.

### Effective date

We believe that the Proposal should be effective at the same time as any new standard and related amendments on using the work of specialists. As described in this letter, if our understanding of the Proposal is correct and changes to it are not made, we believe that its implementation could be a significant undertaking. As a result, we recommend that the standard be effective for audit periods ending two years after the Securities and Exchange Commission approves the final standard.

We would be pleased to discuss our comments with the Board or the PCAOB staff at your convenience.

Very truly yours,

Ernst + Young LLP

Copy to:

**PCAOB**

James R. Doty, Chair
Lewis H. Ferguson, Board Member
Jeanette M. Franzel, Board Member
Steven B. Harris, Board Member
Martin F. Baumann, Chief Auditor and Director of Professional Standards

**Securities and Exchange Commission**

Jay Clayton, Chairman
Kara M. Stein, Commissioner
Michael S. Piwowar, Commissioner
Wesley R. Bricker, Chief Accountant
Marc A. Panucci, Deputy Chief Accountant

**Appendix — Additional observations**

| Comment number | Reference | Observation |
|---|---|---|
| 1 | Proposed AS 2501 .04 | This paragraph indicates that AS 2110, *Identifying and Assessing Risks of Material Misstatement*, establishes requirements regarding the process of identifying and assessing the risks of material misstatement related to accounting estimates. However, it is not clear where such requirements exist in AS 2110. We observe that the proposed amendments to AS 2110.60 and .60A set forth risk factors relevant to the identification of significant accounts and disclosures involving accounting estimates. We are unclear whether the Board intends for auditors to consider these same risk factors when identifying and assessing the risks of material misstatement related to accounting estimates. If so, we believe the Board should clarify its expectations. |
| 2 | Proposed AS 2501 .10 | The note to this paragraph states that evaluating whether the methods are in conformity with the requirements of the applicable financial reporting framework includes evaluating whether the data and significant assumptions are appropriately applied under the applicable financial reporting framework. This requirement is not clear to us, particularly the meaning of the phrase "appropriately applied." We recommend that the Board clarify its intent. |
| 3 | Proposed AS 2501 .11 | This paragraph proposes audit requirements for when the company has changed its method for determining the accounting estimate. We agree with this proposed requirement, but we believe the auditor should also be required to evaluate, if facts and circumstances have changed, whether management failed to revise its method to recognize the new facts and circumstances. We believe such a requirement would highlight the importance of applying professional skepticism when auditing estimates. |
| 4 | Proposed AS 2501 .21 | Paragraph .21 states that developing an independent expectation involves the auditor using some or all of his or her own methods, data and assumptions to develop an expectation of the estimate for comparison to the company's estimate. We agree that performing a calculation of the estimate using some or all of management's methods, data and assumptions and some or all of the auditor's methods, data and assumptions is an important approach for testing certain estimates, especially significant accounting estimates that require complex models or have high estimation uncertainty. However, we believe the phrasing "developing an independent expectation" implies that the auditor would reach this expectation independently, without reference to management's methods, data and assumptions. We do not believe developing a truly independent expectation is consistent with the definition of the procedure as defined in the proposed standard. We recommend that the Board consider changing this phrasing to developing a "comparative estimate" or a "point estimate" to better reflect the procedures described. We also note that ED-540 uses the term "point estimate." |

| Comment number | Reference | Observation |
|---|---|---|
| 5 | Proposed Appendix A of AS 2501 .A1b | In connection with identifying and assessing risks of material misstatement related to the fair value of financial instruments, this paragraph would require the auditor to take into account the extent to which the fair value of a particular financial instrument is based on inputs that are observable directly or indirectly. As described more fully in the above section regarding Proposed Appendix A to AS 2501, we believe the auditor should be permitted to stratify financial instruments into groups as part of identifying and assessing risks of material misstatement. Hence, we suggest the following edit to paragraph .A1b: "The extent to which the fair value of the <u>type of</u> financial instrument is <u>generally</u> based on inputs that are observable directly or indirectly[.]" |
| 6 | Proposed Appendix A of AS 2501 .A4a | This paragraph includes the following factor auditors should consider in assessing the reliability of audit evidence (pricing information) provided by a pricing service: "The experience and expertise of the pricing service relative to the <u>types of financial instruments being valued</u>, including whether <u>the financial instruments being valued</u> are routinely priced by the pricing service[.]" In the second part of the sentence, we believe the requirement should use the phrase "<u>types of</u> financial instruments" instead of "<u>the</u> financial instruments" We believe it could be difficult to determine whether a specific financial instrument is routinely priced by the pricing service. |
| 7 | Proposed Appendix A of AS 2501 .A8a | This paragraph uses terms that are not clearly defined such as recent and substantially similar. If this condition is retained in a final standard, we recommend the Board clarify what would constitute a recent trade and delete the word substantially to be consistent with ASC 820, which uses the term similar. We do not believe the proposal is clear about how an auditor would determine what constitutes substantially similar. |
| 8 | Proposed Appendix A of AS 2501 .A9 | This paragraph discusses relevance and reliability considerations of a broker quote used by the company in measuring the fair value of a financial instrument. It appears the Board intended the guidance in the Appendix to apply when the auditor tests the company's price or uses a company's price when developing an independent expectation. However, the first sentence of proposed paragraph .A9 reads as though this paragraph only applies when the auditor tests the company's price based on a quote from a broker or dealer. We suggest that the Board clarify its intent, especially if the Board intended for. A9 to also apply when auditors develop an independent expectation using a broker quote. |
| 9 | Proposed Appendix A of AS 2501 .A9 | This paragraph provides guidance on how to evaluate the relevance and reliability of a single broker quote. We recommend the Board also provide guidance on how to evaluate the relevance and reliability of multiple broker quotes when not all criteria are met, similar to proposed paragraph .A8 when using pricing information from multiple pricing services. |

| Comment number | Reference | Observation |
|---|---|---|
| 10 | Proposed Appendix A of AS 2501 .A10 | This paragraph includes requirements on auditing unobservable inputs that are significant to the valuation. We believe Proposed AS 2501 addresses these requirements, including those on identifying significant assumptions (paragraph .15) and evaluating the reasonableness of significant assumptions (paragraphs .16–.18). In addition, there are many types of unobservable inputs to financial instruments, so it is not clear to us why .A10 only takes into account modifications made to observable information and whether management appropriately considered the information available. We recommend deleting this paragraph. |
| 11 | Proposed Appendix A of AS 1105 .A2c | This paragraph says the auditor should read the available financial statements of the investee to obtain an understanding of the extent to which the investee's financial condition or operating results affect the valuation of the company's investment. It is not clear to us how the auditor would gain this understanding by reading the investee's financial statements. We believe the auditor would better understand the investee's financial condition by understanding the investor's process, including the methods and assumptions, for determining the value of the investee. Therefore, we recommend that the Board delete section c from proposed paragraph .A2. |