financial executives international

February 18, 2009

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 026

Dear Board:

The Committee on Corporate Reporting ("CCR") of Financial Executives International ("FEI") wishes to share its views on the Public Company Accounting Oversight Board ("PCAOB") Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk ("proposed standards"). FEI is a leading international organization of senior financial executives. CCR is the senior technical committee of FEI, which reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations. This document represents the views of CCR and not necessarily the views of FEI or its members individually.

We believe the proposed standards accomplish the PCAOB's objective of establishing appropriate foundational principles on which future auditing standards can be based. We agree with the Public Oversight Board's Panel on Audit Effectiveness recommendation that "the audit risk model is appropriate, but needs enhancing and updating." A quality audit conducted within a reasonable amount of time and using a rational amount of resources, must be driven by risk assessments that direct the auditor's allocation of effort toward the areas of greatest risk.

Furthermore, we applaud the PCAOB's efforts to improve the requirements related to risk assessment such that they enhance the integration of the audit of the financial statements together with the audit of internal control over financial reporting. This is in alignment with the goal of improving the effectiveness and efficiency of the integrated audits.

The proposed standards include the statement "The auditor should perform substantive procedures for each relevant assertion of each significant account and disclosure, regardless of the assessed level of control risk." To ensure integrated audits of financial statements are of sufficient quality, we strongly agree that the Board's standards governing risk assessments need to contain the statement. However, taken by itself, this powerful statement could be misinterpreted to be inconsistent with an appropriately integrated audit. Accordingly, we suggest the Board add a note to this paragraph that explains why the requirements outlined in this paragraph must be true for a quality integrated audit to be conducted.

Similarly, we trust that the proposed standards will also be explicitly incorporated into the PCAOB's inspection process so as to ensure that auditors are truly implementing the guidelines for an integrated audit. As preparers of financial statements subject to audit under the PCAOB guidelines, one of our concerns is that the principles and objectives of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements (*"AS5") directed towards the achievement of quality, integrated audits are not applied consistently in practice. More specifically, we have concern that at times auditors spend too much time on inconsequential or lower risk areas and conversely do not spend as much time on higher risk, more complicated areas as they should. Accordingly, we believe that such concern could be mitigated and the objectives of AS5 and these proposed standards met if the requirements of the proposed standards be explicitly incorporated into the PCAOB inspection process.

The attachment that follows contains several other less significant suggestions for improvement.

We appreciate the PCAOB's consideration of these matters and welcome the opportunity to discuss any questions you have with respect to our comments.

Sincerely,

Arnold C. Hanish
Chairman, Committee on Corporate Reporting
Financial Executives International

ADDITIONAL COMMENTS ON PROPOSED AUDITING STANDARDS RELATED TO THE AUDITOR'S ASSESSMENT AND RESPONSE TO RISK

We believe there could be enhancements to the proposed standards that would support the PCAOB's goal of improving the effectiveness and efficiency of the integrated audit. We have limited our comments to the following three standards:

- Identifying and Assessing Risks of Material Misstatements
- The Auditor's Responses to the Risks of Material Misstatement
- Consideration of Materiality in Planning and Performing an Audit

Identifying and Assessing Risks of Material Misstatements
We appreciate that the proposed standard is more specific in nature as it should create more consistency in the performance of financial statement audits as well as audits of internal controls by audit firms. This should also allow for more consistent measurement of the audit firms by the PCAOB. However, there are several areas in the proposed standard where we believe more specific verbiage should be considered:

- The standard includes factors and procedures an auditor should consider as part of obtaining an understanding of the company and its environment. We agree the items listed should be considered for all audits. The risk, however, with stating this as a "requirement" is that auditors will approach this as a "check-list" and the substance intended to be gained from such review will not be realized. We are concerned that the standard does not go far enough to connect the level of risk assessment to the substantive audit procedures that need to be performed. To truly ensure an effective and efficient audit, we believe auditors need to be very specific in determining how their time is allocated based on the risk assessment to prevent too much time on low risk accounts and not enough time on high risk accounts.

- We agree with the PCAOB's objective to write the proposed standard primarily from the integrated audit perspective. However, we believe that the note supplementing paragraph 34 seems to contradict the goal of one risk assessment being used for both the audit of the financial statements and the audit of internal controls. More specifically, we do not understand why a broader range of accounts and disclosures needs to be reviewed for the purpose of evaluating the effectiveness of internal control over financial reporting than what is necessary for an audit of financial statements only. Paragraph 7 of the Proposed Standard of Identifying and Assessing Risks of Material Misstatements explicitly states that the risks and risk assessment procedures should be the same for both types of audits.

The Auditor's Responses to the Risks of Material Misstatement
We agree with the proposed standard's guidance on auditor's responses to the risks of material misstatement. However, we believe the standard should include reference to the auditor's ability to use the work of others to obtain evidence about the design and operating effectiveness of controls as stated in AS5.

Consideration of Materiality in Planning and Performing an Audit

We agree with the proposed standard's guidance on establishing a lower materiality level or levels for particular accounts or disclosures, and appreciate the examples listed in the additional discussion of situations in which a lower materiality threshold might be needed. However, we believe the standard could provide additional clarity in the application of materiality in the following areas:

- We recommend that the proposed standard further define how an auditor should determine materiality of an uncorrected misstatement, with the intent of achieving a much greater degree of consistency and reliability of the financial statements being audited. One could argue that the variations in how auditors apply judgment to this metric do not provide consistency to financial statement users.

- Paragraph 5 states, when planning the audit, the auditor's materiality level for the financial statements as a whole be expressed as a specified amount. We believe this statement could also apply to paragraph 7 when assessing materiality for particular high risk accounts or disclosures.