

P B T K

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September 26, 2011

To: Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W., Washington, D.C. 20006-2803
Transmitted by e-mail to: comments@pcaobus.org

Re: PCAOB Rulemaking Docket Matter No. 34
Release No. 2011-003, "Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements"

We appreciate the opportunity to respond to the "Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements" (the Release) that is contained in Release No. 2011-003 dated June 21, 2011, of the Public Company Accounting Oversight Board (the PCAOB or the Board). We note that many of our concerns are already mentioned in the Release and deserve the Board's continuing serious consideration.

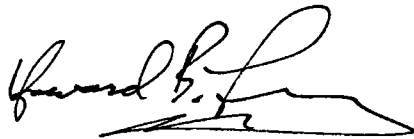
We begin our discussion by setting forth our broad view of the four "alternatives" suggested in the Release as possible ways to achieve the objective expressed in the third paragraph of Part I thereof. Briefly summarized, the four alternatives (reporting Alternative Nos. 1-4) include (1) a required "Auditor's Discussion and Analysis" (AD&A) to provide information about the audit and the financial statements, (2) required expanded use of emphasis paragraphs, (3) reporting on information outside the financial statements, and (4) clarification of certain report language. In short, we would be in favor only of reporting Alternative No. 4. For reasons articulated in the attachment that follows, we would be vigorously opposed to any future proposal that would seek to revise PCAOB standards to include requirements for any of the suggestions in reporting Alternative Nos. 1-3. Moreover, we doubt the validity of the Board's apparent conclusions as to the significance of any investor needs or demand for any such action.

We present details of, and support for, our overriding concerns and reservations in Part 1 of the attachment. In Part 2 we briefly respond to the 32 specific questions posed in the Release. To reduce the need for redundancies, our responses to such questions consist to a large extent of cross-references to relevant paragraphs in Part 1

Thank you for this opportunity to comment. We hope the Board finds our comments useful in its deliberations on this matter. Please contact the undersigned at hlevy@pbtk.com or 702/384-1120 if there are any questions about these comments.

Very truly yours,

Piercy Bowler Taylor & Kern, Certified Public Accountants



Howard B. Levy, Sr. Principal and
Director, Technical Services

Attachment

Part 1 – Overriding Concerns and Reservations

1.1 The Release asserts that it is focused primarily on enhancing communication to investors rather than on changing the fundamental role of the auditor. However, as discussed below, most particularly in paragraph 1.8 (relative to the AD&A discussed as reporting Alternative No. 1), it is our view that new standards such as are under consideration in the Release, with the exception of reporting Alternative No. 4, would, indeed, have the unfavorable effect of fundamentally altering the auditor's role and function.

Demand for change:

1.2 We are far from persuaded and, in fact, have considerable doubt, that there is persuasive evidence currently available of any compelling need or demand among investors and other users for the kind of information that auditors might be required to report as a consequence of this project. We have read some of the early comment letters received from others (for example, the rather typical letter dated July 15, 2011, from the Florida Institute of Certified Public Accountants) and firmly believe that the comment letters ultimately will bear convincing evidence, to a much greater extent than the Board's initial "outreach" efforts did, of the highly controversial level of the conclusions and recommendations embodied in the Release, albeit presented as tentative. Moreover, we believe that the survey-based research about users' needs for possible revisions to PCAOB standards relating to auditor reporting appears most likely flawed seriously in many respects and has resulted in conclusions (again, albeit presented as tentative) that appear inherently biased and, therefore, unreliable. Accordingly, with the possible exception of reporting Alternative No. 4, without significantly more and credible research, we believe it would be extremely premature to take any action at this time on any proposal, even to formally propose such as in an exposure draft standard or series of standards relative to reporting Alternative Nos. 1-3. (See also paragraphs 1.22, 1.24 and 1.26, below, with specific regard to the demand for reporting under reporting Alternative No. 3.)

1.3 Although not presented in the description of the PCAOB staff's "outreach" efforts (Appendix C) included in the Release, we have learned that the survey undertaken was distributed by mail to a relatively small population of 300 consisting primarily of leaders of institutional investors of which 73 (or 24%) responded. Although such a rate of response is not unusually small for any survey, only 45% of the respondents or 11% of the entire population surveyed (*i.e.*, only 33 respondents) expressed any dissatisfaction with the information provided by current audit report model. Accordingly, we believe the frequent use in the Release of the expression, "many investors," constitute a series of overstatements of the facts. We believe that 33 respondents is hardly a significant enough response to reasonably constitute a basis to justify the drastic changes in current practice suggested resulting in a fundamental and significant effect on issuers, their auditors and investors, alike. On the contrary, we believe that the survey results better supports an opposite conclusion because the 227 nonrespondents (or 76% of surveyed population) afford persuasive evidence of a high level of investor indifference to the prospect of introducing new reporting standards that would require such changes, rather than supporting an assertion that there is a substantial demand for it.

1.4 We find it extremely difficult to place any credence in Board's interpretation of these survey results when we factor into this analysis: (a) the probability that the 227 nonrespondents are likely satisfied with (or disinterested in) the content of the standard audit report, or as further evidence of probable investor indifference, considered themselves too busy to respond to the survey, (b) the fact that responses were inherently more likely to be received from those who are, in fact, dissatisfied with the *status quo* than from those who were not, and (c) that human nature being what it is, if you ask someone if (at no cost to them) they want more information than they are currently getting, they will likely respond in a knee-jerk reaction in the affirmative. We believe that the latter most likely accounts for the apparently unanimous support for the AD&A from large investor groups observed at the recent September 15th roundtable discussion – "If you build it, they will come!" This phenomenon may also explain why it is asserted in the Release only that the changes on the reporting model under consideration "might be useful to investors" and that "many investors *are supportive of* changing the auditor's model [emphasis added]" as opposed to more positive statements relative to perceived investor demand for such changes.

1.5 As is evident from the historical discussions in the Release, most particularly Appendix A, the evolution of the standard audit report has been slow and cautious over the past more than 100 years. In the early days of this evolution, standard-setters recognized the importance of eliminating or reducing opportunities for auditors to include vague and inconsistent language in their reports that would not effectively serve the needs of users. The most recent substantive changes in the standard audit report form (*i.e.*, excluding references to PCAOB standards for reporting on financial statements of issuers) were introduced in 1988 in SAS 58 as part of the so-called "expectation gap" standards and were primarily to clarify the auditor's responsibilities and distinguish them from management's. We believe these reporting objectives to be still valid today because sweeping, fundamental and sudden drastic changes in the audit reporting model would be inherently confusing to the investment community and, therefore, disruptive to the capital markets. We would oppose any recommendation, for example, such as for an AD&A, that would move audit reporting in any

direction not consistent with the reporting objectives discussed in this paragraph. Accordingly, we believe considerably more evidence of the presence of a compelling demand should be necessary to support continuing efforts to produce a future proposal for such fundamental changes in the role of auditors and the nature of their reports.

Role and authority of PCAOB:

1.6 The Release causes one to question whether a forthcoming proposal from the PCAOB to adopt the suggested revisions to the standards might, in some ways, exceeds its statutory authority under the federal Sarbanes-Oxley Act of 2002 (the Act). It appears that Sections 101(a) and (c) (5) and 103(a)(1) and (4) of the Act contain broad enough language that could enable an interpretation that such action would be within the Board's authority. Nevertheless, it remains a question as to whether Congress ever intended the PCAOB's role or authority to go significantly beyond (a) setting the standards for performing audit and other services that issuers are already required under the federal securities laws or might optionally engage auditors to perform, (b) qualifying auditors through the registration process to perform such services, (c) monitor the performance of such services through its inspection process, and (d) impose disciplinary actions against noncompliant or incompetent auditors.

1.7 As discussed in more detail below, we believe that requirements such as those suggested for consideration by reporting Alternative Nos. 1 and 3 would be beyond our understanding of the probable intent of Congress as to the role and authority of the Board because they would set auditor's reporting responsibilities so far outside those requirements that are presently embodied in the federal securities laws, as now constituted, and the traditional auditor's role. Accordingly, if such requirements are ever to be included in standards applicable to auditors, we believe they should be initiated by actions of the U.S. Securities and Exchange Commission (SEC) under specific Congressional authority preferably to be derived from legislation not yet enacted.

Alternative No. 1 (the AD&A):

1.8 Expanding on the idea introduced above in paragraph 1.1, we believe any proposal to require auditors to issue AD&As under reporting Alternative No. 1 (clearly the most objectionable among the four presented) would likely have the generally undesirable effect of fundamentally changing and expanding the role of an auditor beyond that of an attester to the reliability of management's (*i.e.*, to add credibility to those assertions, most significantly, for example, as to fair presentation of the financial statements and accompanying note disclosures) to be more like that of a regulator, overseer, critic and/or whistleblower or adversary. This change in reporting responsibility would likely have the more specific undesirable effect, among others discussed below, of engendering management distrust of the auditors and consequently impairing working relationships and the open, unfiltered communications that are necessary to enable the effective and timely completion of a financial audit as we now know it. Further, we believe that public disclosure of matters that are now or should now be disclosed only to audit committees confidentially for them to act upon in exercising their oversight functions will likely put undue pressure on such committees and certain auditor disclosures might be viewed as providing a basis for criticizing audit committees, thus straining relationships between their members and the auditors as well.

1.9 Auditing is a highly complex professional discipline that requires years of education, training and experience to enable appropriate judgments as to risk assessment and audit scope in any given set of circumstances. Historically, we have seen countless examples of expert witnesses disagree on matters of risk assessment and audit scope adequacy and in recent years, substantial evidence of such disagreements between knowledgeable, experienced professionals is publicly available in the reports of PCAOB inspections and responses thereto. Accordingly, we believe that public disclosure of details of risk assessments and audit scope would not serve any useful purpose but rather would diminish the value of an audit report as such details would not only exceed the capabilities of investors and other users to make meaningful assessments and useful judgments about but also quite probably would be misunderstood and/or confusing to most of them. It is unreasonable, in our opinion, to create expectations that any form of written report, no matter how expanded it is from the current model, that is inherently limited by time and space, would enable lay users to make meaningful judgments as to such complex matters as would relate to the appropriate audit risks and scope.

1.10 Because of the almost endless variety of matters that might be included in an AD&A, if even a reasonably consistent structure or format were to be prescribed by a future standard, we firmly believe the language to be contained therein would necessarily be nonstandard. We also believe that, depending upon the writing style preferences and skills of individual auditors or their firms, such nonstandardized, free-form audit reports, in general (*i.e.*, even as to matters other than audit risk and scope), would not afford any measurable benefits to investors or other users because, at best, most likely, such reports would be readily misunderstood and extremely difficult for such users either to interpret or to make meaningful comparisons among reports on financial statements of different issuers that represent alternative investment opportunities under consideration.

1.11 It appears that an AD&A prepared under reporting Alternative No. 1 would be a throwback to an old, and similarly nonstandardized reporting format called the “long-form” report that was initially “officially” legitimized in 1957 in Statement on Auditing Procedure (SAP) No. 27 after many years of common use. In 1957, the long-form report was often issued either in addition to, or instead of, the so-called “short-form” report or “certificate,” which was first formally standardized in 1948 in SAP 24 and designed to meet consistently the minimum requirements of the reporting standards contained in the nine (later expanded to ten) “generally accepted auditing standards” that were adopted that year. In connection with long-form reports, SAP 27 provided little or no specific guidance as to form and content except to caution auditors wisely against certain risks associated with such reporting by emphasizing (a) the need to maintain a “clear-cut distinction” between representations of management and the auditors (b) the fact that “comments or other data contained in the long-form report [may] lend themselves to a contention that they constitute exceptions or reservations, as distinguished from mere explanations,” and (c) that client financial information contained in such a report may “support a contention that the auditor has made *factual* representations rather than express an *opinion*... [on] management representations.” We believe these risks would re-present themselves and would remain significant in the event any form of reporting Alternative No. 1 were to be required (or even made optional) for public reporting purposes.

1.12 Although required to maintain objectivity and be independent in both fact and appearance (as independence has effectively been defined in a long series of rules, interpretations, rulings and regulations of various bodies), it remains a fact of professional life that auditors compete with one another for clients. One way they are able to compete while remaining within the restrictive boundaries of independence, is to offer their clients value-added suggestions for improving, for example, their operating efficiency and, thus, profitability.* In the face of an AD&A reporting responsibility, as mentions in SAP 27, many such recommendations may likely bear a significant risk of being inappropriately viewed as exceptions or criticisms if included an AD&A and may, therefore, be withheld and be adverse to the economic best interests of the issuer and its investors.

1.13 Over time, following the issuance in 1957 of SAP 27, the use of long-form reports diminished quickly and greatly in practice, particularly as an alternative for what, in contrast, was still called a “short-form” report. However, beginning with Statement on Auditing Standards (SAS) No. 2, issued in 1974, the short-form report was formally redesignated the “standard” audit report, and effectively, use of the long-form report as an alternative to it was no longer deemed acceptable. Although the long-form report continued to be available for use as a type of supplemental report, it was rarely issued thereafter for distribution to other than a select group of users, its use has virtually vanished from modern practice largely, we believe, most likely in recognition of the risks set forth in SAP 27 and other reasons presented elsewhere in this discussion (not the least of which was likely a growing concern for the liability risk discussed in the next paragraph). We do not believe there is any compelling reason at this time to bring the long-form report back as an AD&A.

1.14 We see it as frightening to consider the enormous exposure to liability for auditors presented by long-form type reporting in our nation’s highly litigious culture, and in today’s economic and political environment that tends to generate extreme market price volatility, given the improbability of developing sufficiently rigid standards at least as to form and general content, if not specific standard language. Such risk relates not just to what an audit firm might include in, but to what it might exclude from, its report. In fact, we believe such risk is likely to result in firms, particularly the large firms, adding multiple layers of review to the audit reporting process so as to seriously impair their ability to issue reports timely and also would add costs that are not commensurate with any realizable benefits to issuers or others that would be better spent in operations, thus adding real value indirectly to the interests of investors.

1.15 Although we recognize as worthwhile the objective of making the standard audit report more informative (such as in accordance with reporting Alternative No. 4, if proposed), we believe that human nature is such that if audit reports were to become too long (say, more than one page), the probability of them being read and effectively achieving any meaningful communication objective would likely diminish severely. We note that in the PCAOB staff’s outreach survey, it was determined that a large proportion of the investors who responded do not currently read standard audit reports, but we believe that phenomenon is more likely attributable to their familiarity than to dissatisfaction with its content or to or disinterest therein.

1.16 Audit committees generally have at least one member who qualifies under a regulatory definition of “financial expert,” and as pointed out by Cynthia M. Fornelli on p. 3 of her letter that was issued on behalf of the Center for Audit Quality and dated June 9, 2011, (prior to issuance of the Release), are expected, as part of their oversight responsibilities, to engage in two-way dialog with auditors in which dialog questions are raised and written

* Depending on the outcome of the Board’s audit firm rotation project now under way, the significance of the economic dynamics of auditor competition to this matter could decline materially with regard to SEC practice. We intend to present our views on the rotation matter in a future comment letter.

communications are clarified and elaborated upon with explanations as may be deemed necessary. Of course, public investors clearly do not have such access to auditors. Accordingly, we believe that auditor communications such as an AD&A as suggested by reporting Alternative No. 1 should be made only to audit committees.

1.17 The Release cites increased transparency for the benefit of investors and other users as an objective. Nevertheless, audit committees, which are charged with financial oversight responsibilities (undoubtedly for the primary purpose of protecting the interests of investors), including assessing the quality and scope of work performed by the independent auditors, have never been made accountable publicly so as to make transparent the scope and results of their oversight activities and provide assurance that investors may rely upon. We believe, if there is determined, in fact, to be a significant demand among investors and other users for the type of information such as an AD&A might provide, it may be time to add some transparency to the work of audit committees by making them accountable with periodic reporting to the public for that which they are supposed to be held responsible. Of course, such a requirement could not come from the PCAOB but rather from Congress and/or the SEC.

Alternative No. 2 (emphasis paragraphs):

1.18 We believe it should continue to be management's, not the auditor's, responsibility to communicate adequately matters necessary to assure an understanding by users of the financial statements. It has long been the auditor's obligation, on the other hand, to assess the adequacy of management's disclosures not only with respect to the requirements of specific accounting standards applicable in the circumstances but to judge whether they are sufficiently clear, complete and not misleading, and to report any exceptions not corrected to the auditors' satisfaction. If this obligation is deemed not widely understood or appreciated by the investment community, we are in favor of expanding the standard audit report, as discussed in the Release in connection with reporting Alternative No. 4, to require clear articulation of this responsibility in the reporting model. We believe that if the auditor meets this responsibility effectively, there ordinarily should be no reason to summarize, supplement or emphasize matters adequately disclosed by management disclosures merely for the purpose of making audit reports unnecessarily "more informative."

1.19 Historically, in addition to the requirement for expressing substantial doubt as a result of a going concern uncertainty, auditors have generally limited the relatively rare use of optional emphasis paragraphs to highlight such potentially sensitive matters that, solely at the auditor's discretion, they have judgmentally deemed sufficiently important, to call to users' attention without an opinion qualification. In its so-called "clarity standards" (issued but not yet effective), the AICPA's Auditing Standards Board (ASB) has elevated the use of such discretion to be characterized in the future as a so-called "requirement" that nevertheless remains solely a matter of auditor judgment with these words: "If the auditor considers it necessary to draw users' attention to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements, the auditor should include an emphasis-of-matter paragraph." However, although examples for consideration are presented in the ASB standard, it still does not require any specific type of matter to be the subject of an emphasis paragraph in audit reports on financial statements of nonissuers. We believe such a requirement to use professional judgment without mandating emphasis paragraphs continues to be appropriate.

1.20 We believe that additional mandatory and expanded use of emphasis paragraphs, such as are suggested in the Release's discussion of reporting Alternative No. 2 would likely have the undesirable effect of diluting the auditor's message, confusing users and diminishing the apparent significance of matters more appropriately communicated by auditors, including the auditor's opinion, (see also paragraph 1.15, above).

1.21 Further, we believe that to mandate the expanded use of explanatory paragraphs would also likely have the undesirable effects of tending to (a) transfer the primary duty of clear disclosure of significant matters to the auditors from management (where it belongs) thus encouraging investors and other users to read only the auditors' most likely summarized discussions of such matters ignoring management's more comprehensive and fully detailed discussions, and (b) like the old long-form report (discussed in paragraphs 1.11-1.15), blur the distinction between representations of management and those of the auditors or be misconstrued by and confuse users as qualifications of, or contradictions to, an audit opinion, or in the absence of an qualified opinion, some comments might be misconstrued as a piecemeal opinion. Our comments above, objecting to public disclosure of matters of audit risk assessment and scope (relative to reporting Alternative No. 1) in paragraph 1.9 apply likewise to such disclosure if made in connection with Alternative No. 2.

Alternative No. 3 (matters outside the financial statements):

1.22 As mentioned in the Release, since 1998, auditors have had a standard (Statement on Standards for Attestation Engagements (SSAE) No. 8 [revised and recodified by SSAE 10 and now PCAOB Interim Attestation Standard AT 701] which we believe adequately governs and provides detailed guidance on the conduct of optional engagements and related

reporting for providing assurance by auditors on a management's discussion and analysis (MD&A) included in an SEC filing. However, in the 13 years since the adoption of SSAE 8, very few such reports have been issued. Repeated requests of Congress and/or the SEC to require auditor attestation on the MD&A have been rejected or ignored over the years. Moreover, a succession of extensions of the effective date from the requirements of Section 404(b) of the Act for auditors' reports on internal control was eventually followed by a permanent exemption for smaller reporting companies. We believe a requirement for auditor attestation on data such as non-GAAP performance metrics would tend to present the undesirable risk of elevating the relevance and significance of such measurements while at the same time detracting from those of GAAP-consistent metrics.

1.23 It is certain that a requirement to extend auditor assurance to matters outside the financial statements would add considerable cost to issuers' compliance, depending on the nature and extent of the subject matter of such additional assurance (and with questionable benefits, as discussed at greater length in paragraphs 1.2-1.4). Also depending on the nature and extent of the subject matter, audit firms might likely have to hire and train additional staff and further disrupt issuers' operations by taking up additional space and time with the latter quite likely reducing their ability for timely financial reporting.

1.24 As discussed in the Release in connection with reporting Alternative No. 4, we are in favor of requiring auditors to better inform investors by including language in standard audit reports regarding their responsibility under AU 550, to read and consider whether information included in an SEC filing is materially inconsistent with the financial statements or other information obtained in the audit or is otherwise misleading. Of course, this responsibility is not applicable to earnings releases. We are not in favor of public auditor association with earnings releases, in large part because of an apparent perceived demand, in many cases, for timeliness of this kind of financial information such that it needs to be disseminated on a preliminary basis prior to the completion of the annual audit. User appetite for timeliness appears to override, and be with full understanding of, the risk that late adjustments might possibly arise that would cause the information to require modification. But we are in favor of a standard that would caution auditors in to read such releases (preferably prior to issuance) and to consider taking appropriate action in the event they appear to be unclear, inconsistent, false or misleading.

1.25 In the event it is ultimately deemed necessary to extend auditor attestation over disclosure matters currently presented outside the financial statements (*e.g.*, non-GAAP performance metrics), consistent with one of the comments of Dennis Beresford (most of which we are in full agreement with) contained in his letter to the Board of July 21, 2011, we assert that it would be relatively easy for the SEC to either cause the Financial Accounting Standards Board to sweep such disclosure matters into its current body of accounting standards or to supplement such accounting standards applicable to issuers as it has many times in the past. Thus, we believe there is no need to layer on additional auditor reporting as described under reporting Alternative No. 3 to cover matters that could be addressed in this fashion.

1.26 All of this, in our opinion, constitutes persuasive evidence of a relatively low level of investor demand or sense of need at this time to expand auditor reporting into information that is presented outside the financial statements. Accordingly, we do not believe a standard that would require such reporting should be proposed or adopted by the Board unless and until initiated by the SEC but only after duly considering and ruling out the alternative approach suggested in the preceding paragraph and following additional, more extensive research, including a period of experimentation through encouragement of voluntary compliance. The foregoing notwithstanding, we adequately would be in favor of developing and issuing performance and reporting standards for engagements to be entered into and conducted solely at the discretion of the client that would provide auditor assurance as to matters of disclosure made outside the financial statements.

Alternative No. 4 (clarifying language):

1.27 Although we are not in favor of altering the reporting model in any of the ways contemplated by reporting Alternative Nos. 1-3, we are in favor of clarifying matters auditors are already reporting upon that would improve the understandability of audit reports and, therefore, their usefulness for making investment decisions (provided the added report language does not speak directly to matters of specific audit risks and scope).

1.28 Consequently, in accordance with our afore-mentioned view (paragraph 1.5) that the evolution of the audit reporting model should remain (a) slow and cautious as it has been historically, and (b) consistent with the objectives of SAS 58 and the other "expectation gap" standards issued in 1988, we believe that reporting Alternative No. 4 has considerable merit and, thus, represents the only one of the four presented in the Release that clearly warrants further consideration at this time.

Part 2 – Responses to Specific Questions Presented in the Release

We believe we have addressed in the foregoing comments (Part 1) most, but not all, of the specific questions presented in the Release (and below). Nevertheless, in Part 2, to facilitate the analysis and summary by the PCAOB staff of the comments received, we have addressed these questions using parenthetical references to our relevant comments in Part 1, wherever applicable, that we believe are most directly responsive to the questions.

Q1. 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?

No. We believe the Board should undertake a standard-setting initiative at this time to consider improvements that would be limited only as set forth below under *Q1b*. (1.1-1.17)

b. In what ways, if any, could the standard auditor's report or other auditor reporting be improved to provide more relevant and useful information to investors and other users of financial statements?

We believe any standard-setting initiative to be undertaken at this time should consider improvements only with regard to reporting Alternative No. 4. (1.1-1.17 and 1.27-1.28)

c. Should the Board consider expanding the auditor's role to provide assurance on matters in addition to the financial statements? If so, in what other areas of financial reporting should auditors provide assurance? If not, why not?

No. We do not believe the Board should consider expanding the auditor's role to require issuing assurance on matters presented outside the financial statements. (1.22-1.26)

Q2. 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? If not, why not, and what changes are needed?

Yes. We believe that the current so-called "pass/fail" audit report form continues to be appropriate and should not be changed. We believe the introduction of gradations within the "pass" condition will likely be inherently difficult, if not impossible, for by users to interpret consistently as intended and, therefore, most probably will be misunderstood and of no value to the investment community.

b. If the pass/fail model were retained, are there changes to the report or supplemental reporting that would be beneficial? If so, describe such changes or supplemental reporting.

No. See our response to *Q2b*.

Q3. 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.

As stated in the "overall philosophy" contained in the September 8, 2011, e-mail comments to the Board of Arthur Siegel (which, incidentally, contains many insightful comments with which we concur), we firmly believe that to maintain the proper clear distinction between representations of management and the auditors, reports of independent auditors should continue to be limited to matters relevant to attesting to the reliability of those management assertions. Accordingly, we believe that, to the extent information about the issuer's financial statements is not provided pursuant to the SEC's requirements for the MD&A, it should be provided by management and/or the audit committee, as appropriate. (1.8 and 1.18-1.21)

Q4. *Some changes to the standard auditor's report could result in the need for amendments to the report on internal control over financial reporting, as required by Auditing Standard No. 5. If amendments were made to the auditor's report on internal control over financial reporting, what should they be, and why are they necessary?*

Our opposition to introducing details of auditor judgments about risk assessments and scope determination in an audit report would apply equally to reports that attest to the effectiveness of internal control over financial reporting (ICFR). The type of changes that we would favor (*i.e.*, those that are described in reporting Alternative No. 4) would not be necessary with regard to the ICFR portion of a combined report on financial statements and ICFR (the most prevalent choice) but might likely be applicable in some respects for a separate ICFR report issued pursuant to AS5.

Because of our views, we choose not to respond with regard to any changes that might be proposed and be related to reporting Alternative Nos. 1-3.

Q5. *Should the Board consider an AD&A as an alternative for providing additional information in the auditor's report?*

No. We are equally opposed to the AD&A whether as either a component of, or supplement to, a standard audit report. See our response to **Q1a.** (1.8-1.17)

a. *If you support an AD&A as an alternative, provide an explanation as to why.*

Not applicable. See our response to **Q5.** (1.8-1.17)

b. *Do you think an AD&A should comment on the audit, the company's financial statements or both? Provide an explanation as to why. Should the AD&A comment about any other information?*

Not applicable. See our response to **Q5.** (1.8-1.17)

c. *Which types of information in an AD&A would be most relevant and useful in making investment decisions? How would such information be used?*

Not applicable. See our response to **Q5.** (1.8-1.17)

d. *If you do not support an AD&A as an alternative, explain why.*

See our response to **Q5.** (1.8-1.17)

e. *Are there alternatives other than an AD&A where the auditor could comment on the audit, the company's financial statements, or both? What are they?*

No. We do not believe that public disclosure by auditors of details about judgments about risk assessments and scope is appropriate in any circumstances. We do believe, however, that audit committees should be required to disclose that they are satisfied with the significant auditor judgments about risk and scope and describe, in general terms, the basis for their conclusions. A requirement for such reporting by the audit committee should not come from the PCAOB. (1.9, 1.16-1.17)

For comments about the financial statements, see our response to **Q3.** (1.8 and 1.18-1.21)

Q6. *What types of information should an AD&A include about the audit? What is the appropriate content and level of detail regarding these matters presented in an AD&A (i.e., audit risk, audit procedures and results, and auditor independence)?*

Not applicable. See our responses to **Q5a-f.** (1.8-1.17)

Q7. *What types of information should an AD&A include about the auditor's views on the company's financial statements based on the audit? What is the appropriate content and level of detail regarding these matters presented in an AD&A (i.e., management's judgments and estimates, accounting policies and practices, and difficult or contentious issues, including "close calls")?*

As we have previously stated, we do not believe it is appropriate for an auditor to report publicly views on the issuer's financial statements beyond an opinion attesting to the fairness of management's assertions embodied therein or any reservation or exceptions thereto (which, of course, would not be acceptable to the SEC). We believe the capital

markets would likely be disrupted and not be well served by either auditors or management reporting what might be called "close calls" once they have been resolved to the satisfaction of the auditors and the audit committee because such reporting might likely cause inappropriate doubts about the reliability of the management assertions embodied in their financial statements and likely be misconstrued as qualifications of, or contradictions to, an audit opinion (or, once again, in the absence of an qualified opinion, some comments might be misconstrued as a piecemeal opinion). (1.8, 1.11, 1.18-1.21)

Q8. *Should a standard format be required for an AD&A? Why or why not?*

Not applicable. See our responses to **Q5a-f.** (1.8-1.17)

Q9. *Some investors suggested that, in addition to audit risk, an AD&A should include a discussion of other risks, such as business risks, strategic risks, or operational risks. Discussion of risks other than audit risk would require an expansion of the auditor's current responsibilities. What are the potential benefits and shortcomings of including such risks in an AD&A?*

Even if an AD&A were to be required by a future standard, to which we are opposed, we would likewise be opposed to public disclosure of such additional risk matters as we believe it would not be understandable by investors or other users in a way that would help them make intelligent investment decisions. See our responses to **Q5a-f.** (1.8-1.17)

Q10. *How can boilerplate language be avoided in an AD&A while providing consistency among such reports?*

Because of the wide variety of possible matters that would be reported in an AD&A contemplated by reporting Alternative No. 1, if adopted in a future standard, we are unable to the development of any significant "boilerplate" language imagine at this time for use in an AD&A or to otherwise provide for consistency in reporting therefor. (1.10)

Q11. *What are the potential benefits and shortcomings of implementing an AD&A?*

We believe there would be no meaningful benefit to investors or others if a requirement to issue AD&As were adopted. See our responses to **Q1a-f.** (1.8-1.17)

Q13. *Would the types of matters described in the illustrative emphasis paragraphs be relevant and useful in making investment decisions? If so, how would they be used?*

We believe that an emphasis paragraph regarding substantial doubt as to a going concern uncertainty should continue to be the only mandatory one. The use of other emphasis paragraphs should continue to be rare and at the reporting auditor's discretion based solely on judgmental considerations about sensitivity and significance. Emphasis paragraphs should not be used indiscriminately to supplement or explain management's disclosures once deemed to be adequate. (1.18-1.21)

Q14. *Should the Board consider a requirement to include areas of emphasis in each audit report, together with related key audit procedures?*

No. See our response to **Q13.** (1.18-1.21)

a. *If you support required and expanded emphasis paragraphs as an alternative, provide an explanation as to why.*

Not applicable. See our response to **Q13.** (1.18-1.21)

b. *If you do not support required and expanded emphasis paragraphs as an alternative, provide an explanation as to why.*

See our responses to **Q1a-b, Q5e** and **Q13.** (1.1-1.21)

Q15. *What specific information should required and expanded emphasis paragraphs include regarding the audit or the company's financial statements? What other matters should be required to be included in emphasis paragraphs?*

Not applicable. See our response to **Q13.** (1.18-1.21)

Q16. *What is the appropriate content and level of detail regarding the matters presented in required emphasis paragraphs?*

Although we do not believe the required use of emphasis paragraphs should be expanded, if they were, we would not be in favor of any level of detail that would exceed the level customarily in use in today's audit reporting model especially if there is a perceived risk that additional explanatory language might likely be misconstrued as qualifying or contradicting an audit opinion. (1.21)

Q17. How can boilerplate language be avoided in required emphasis paragraphs while providing consistency among such audit reports?

Similar to our response to *Q10* relative to an AD&A, because of the wide variety of possible emphasis paragraphs contemplated by reporting Alternative No. 2, if adopted in a future standard, we are unable to the development of any significant "boilerplate" language imagine at this time for use in an AD&A or to otherwise provide for consistency in reporting therefor. See also our responses to *Q5a-f*. (1.10)

Q18. What are the potential benefits and shortcomings of implementing required and expanded emphasis paragraphs?

See our response to *Q13*. (1.18-1.21)

Q19. Should the Board consider auditor assurance on other information outside the financial statements as an alternative for enhancing the auditor's reporting model?

No. (1.22)

a. If you support auditor assurance on other information outside the financial statements as an alternative, provide an explanation as to why.

Not applicable. See our response to *Q19*. (1.22)

b. On what information should the auditor provide assurance (e.g., MD&A, earnings releases, non-GAAP information, or other matters)? Provide an explanation as to why.

None. See our response to *Q19*. (1.22-1.26)

c. What level of assurance would be most appropriate for the auditor to provide on information outside the financial statements?

None. See our response to *Q19*. (1.22)

d. If the auditor were to provide assurance on a portion or portions of the MD&A, what portion or portions would be most appropriate and why?

We are in favor of permitting auditor association with the MD&A (pursuant to AT 701) to remain solely a matter of issuer discretion and, based on our response to *Q19f*, below, we see no reason to divide it into segments that auditors would or would not be required to report upon. If, on the other hand, such a division were to be made, we would recommend that priority for auditor reporting be given (not necessarily in this order) to the comparative results of operations analysis, critical accounting policies and estimates, recent accounting pronouncements, and liquidity and capital resources portions of the MD&A.

e. Would auditor reporting on a portion or portions of the MD&A affect the nature of MD&A disclosures? If so, how?

We understand the MD&A disclosure requirements to be determined by the SEC and its staff and do not understand how they should be affected by the nature and extent of auditor association as a result of attestation services except if divided, to organize the portions such that it is clear to readers which parts are covered by auditor assurance and which are not.

f. Are the requirements in the Board's attestation standard, AT Sec. 701, sufficient to provide the appropriate level of auditor assurance on other information outside the financial statements? If not, what other requirements should be considered?

We believe AT 701 is appropriate and adequate for reporting on the entire MD&A, for which it was designed and intended, but that more tailored standards would likely be required for other applications, depending on the specific nature of other information to be reported on. (1.22)

g. If you do not support auditor assurance on other information outside the financial statements, provide an explanation as to why.

See our response to **Q19**. (1.22-1.26)

Q20. *What are the potential benefits and shortcomings of implementing auditor assurance on other information outside the financial statements?*

We see no meaningful benefits likely to be realized by mandating auditor assurance on disclosures outside the financial statements, only shortcomings, principally the expenditure of company resources that would be unnecessary because of the absence of a demonstrable need. (1.22-1.26)

Q21. *The concept release presents suggestions on how to clarify the auditor's report in the following areas:*

- *Reasonable assurance*
- *Auditor's responsibility for fraud*
- *Auditor's responsibility for financial statement disclosures*
- *Management's responsibility for the preparation of the financial statements*
- *Auditor's responsibility for information outside the financial statements*
- *Auditor independence*

a. Do you believe some or all of these clarifications are appropriate? If so, explain which of these clarifications is appropriate? How should the auditor's report be clarified?

We believe auditor communications would be improved by adding brief explanatory language in the standard report (say, one sentence or two) for each of the foregoing subjects. We also believe the Board should give consideration to requiring the addition of captions such as contained in the ASB's clarity standards" recently issued but not yet effective to aid users to understand and easily read auditor's reports. (ASB) (1.27)

b. Would these potential clarifications serve to enhance the auditor's report and help readers understand the auditor's report and the auditor's responsibilities? Provide an explanation as to why or why not.

Yes. (1.9 and 1.27-1.28)

c. What other clarifications or improvements to the auditor's reporting model can be made to better communicate the nature of an audit and the auditor's responsibilities?

We believe that definitions of the terms, "fairly presented," and "material misstatement," should be considered in addition to the list presented in **Q21**.

d. What are the implications to the scope of the audit, or the auditor's responsibilities, resulting from the foregoing clarifications?

We believe that adding to the standard audit report the foregoing clarifications of such terms and responsibilities, as they are presently understood by auditors, should have no effect on the scope of an audit conducted in accordance with currently applicable auditing standards.

Q22. *What are the potential benefits and shortcomings of providing clarifications of the language in the standard auditor's report?*

We believe the suggested clarifying the language in a standard auditor's report, and possibly adding captions, would make considerable progress in closing the expectation gap. We see no shortcomings of such a change unless the prescribed clarifying language were include discussion of specific risks and matters of audit scope or otherwise be too long and complex so as to impair or diminish the probability of being read or easily understood by users.

Q23. *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?*

As we have stated in many previous responses, we are in favor only of reporting Alternative No. 4. In this case, see particularly our response to *Q1a-b*. (1.1-1.17 and 1.27-1.28)

Q24. 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?

No. See our response to *Q23*.

Q25. What alternatives not mentioned in this concept release should the Board consider?

Not applicable. As we have stated in many previous responses, we are in favor only of reporting Alternative No. 4. In this case, see particularly our response to *Q1a-b*. (1.1-1.2)

Q26. Each of the alternatives presented might require the development of an auditor reporting framework and criteria. What recommendations should the Board consider in developing such auditor reporting framework and related criteria for each of the alternatives?

As we have stated in many previous responses, we are in favor only of reporting Alternative No. 4, to which we are limiting our response. In this case, see particularly our response to *Q22*.

Q27. Would financial statement users perceive any of these alternatives as providing a qualified or piecemeal opinion? If so, what steps could the Board take to mitigate the risk of this perception?

See our responses to *Q7* and *Q16*. (1.11-1.12 and 1.21)

Q28. Do any of the alternatives better convey to the users of the financial statements the auditor's role in the performance of an audit? Why or why not? Are there other recommendations that could better convey this role?

As we have stated in many previous responses, we believe only reporting Alternative No. 4 effectively serves to better users' collective understanding of the auditor's role while Alternative Nos. 1-2 would most certainly add to users' confusion. (Alternative No. 3 would do neither.) See our responses to *Q1a-b*, *Q21a-b*, *Q22* and *Q31a*. (1.5, 1.8-1.12, 1.15-1.18 and 1.20-1.21)

Q29. What effect would the various alternatives have on audit quality? What is the basis for your view?

We believe that none of the alternatives presented would have a measurable effect on audit quality relative to financial statements since, as presented, they would not add to or reduce audit procedures relative to the audit of the financial statement or, if applicable, ICFR. Only reporting Alternative No. 3 would require additional procedures to enable assurance on matters not now covered by an audit opinion. Our views on this matter (like all others expressed in this letter) are based primarily on decades of experience as auditors.

Q30. Should changes to the auditor's reporting model considered by the Board apply equally to all audit reports filed with the SEC, including those filed in connection with the financial statements of public companies, investment companies, investment advisers, brokers and dealers, and others? What would be the effects of applying the alternatives discussed in the concept release to the audit reports for such entities? If audit reports related to certain entities should be excluded from one or more of the alternatives, please explain the basis for such an exclusion.

Since it is our belief that only reporting Alternative No. 4 continue to be under consideration for any future proposed standard, we believe any standard that results from such continuing consideration should be applicable to all entities who are now or will become subject to the reporting requirements of PCAOB auditing standards, If such requirements are to be extended in the future to entities not yet covered, they should be limited to those whose securities are traded in the capital markets.

Q31. This concept release describes certain considerations related to changing the auditor's report, such as effects on audit effort, effects on the auditor's relationships, effects on audit committee governance, liability considerations, and confidentiality.

a. *Are any of these considerations more important than others? If so, which ones and why?*

Yes. As we have stated in many previous responses, we are in favor only of reporting Alternative No. 4. See our responses to *Q1b* and *Q31c*. We have ranked our responses to *Q31c* in categories in the order of importance with the considerations in category 1 seen as the most important primarily because of changing the fundamental role of auditors and their potential for confusing users. (1.1, 1.8-1.12, 1.15-1.18, 1.20-1.21 and 1.26)

b. If changes to the auditor's reporting model increased cost, do you believe the benefits of such changes justify the potential cost? Why or why not?

We believe the costs associated with reporting Alternative No. 4 to be nominal and the benefits, therefore, worth in excess thereof. Although the costs that we believe would be associated with reporting Alternative No. 2 would likely be slightly greater, but probably still nominal, we see no significant benefit but rather several disadvantages (as previously stated) to be obtained from its adoption. On the other hand, we believe the costs that would be association with either of reporting Alternative Nos. 1 or 3 would be considerable, again with no significant benefits (and several disadvantages as previously stated) to be obtained from adoption of either. (1.14 and 1.23)

c. Are there any other considerations related to changing the auditor's report that this concept release has not addressed? If so, what are these considerations?

Among others addressed briefly in the Release, we have mentioned in Part 1 of this letter our reservations and concerns over such matters as may be grouped into four broad categories as follows:

- 1) Changing the fundamental role of the auditor vs. those of management and the audit committee, and the related risk of increasing rather than reducing user misunderstandings thereof (1.1, 1.8-1.12, 1.15-1.18, 1.20-1.21 and 1.26)
- 2) Questions as to reliability of the "outreach" efforts undertaken and the related conclusions drawn regarding investor demand for the types of auditor communications now under consideration (1.2-1.5)
- 3) Questions as to whether the Board is proceeding with too much haste and overstepping its role and authority, as intended by Congress (1.5-1.7)
- 4) Whether such new reporting responsibilities now under consideration (particularly under reporting Alternative Nos. 1-3) would likely damage relationships between auditors and management and between auditors and audit committees that would tend to impair communications and, hence, auditors' ability to conduct high quality audits. (See our response to *Q32*.)

d. What requirements and other measures could the PCAOB or others put into place to address the potential effects of these considerations?

As we have stated in many previous responses, we are in favor only of reporting Alternative No. 4. In this case see particularly our response to *Q1b*.

Q32. The concept release discusses the potential effects that providing additional information in the auditor's report could have on relationships among the auditor, management, and the audit committee. If the auditor were to include in the auditor's report information regarding the company's financial statements, what potential effects could that have on the interaction among the auditor, management, and the audit committee?

We believe that new public auditor reporting responsibilities such as are now being considered under reporting Alternative Nos. 1 and 2 have considerable potential for being viewed as providing investors with a basis for criticism or distrust causing relationships among auditors management and audit committees to become more adversarial and guarded thus impairing working relationships and the open, unfiltered communications that are necessary to enable the effective and timely completion of a financial audit, and additional costs likely to be associated primarily with reporting Alternative No. 3 will further strain such relationships. (1.8, 1.12, 1.14 and 1.23)