

August 15, 2016

PCAOB
Attn: Office of the Secretary
1666 K Street NW
Washington, D.C. 20006-2803

Dear Board Members:

Regarding Rulemaking Docket Matter No. 034, first allow me to express my appreciation not only for the Board's willingness to reexamine one of the most critical components of a set of financial statements to ensure that its potential usefulness is maximized, but also for granting the public the opportunity to provide comments on the proposal. I believe there is great value in reexamining the most significant and enduring piece of communication between independent auditors and the governing bodies whom they serve.

In reading the proposed auditing standard, I see several individual proposals that I would consider to be useful and relevant to investors and other financial statement users, including the following:

- **Independence statement:** As independence between an external auditor and the company it audits is foundational to the provision of reasonable assurance over the material accuracy of the financial statements, I welcome the addition of this statement to the audit report. I think the addition of this language affirms for the readers of the financial statements that this critical aspect of the relationship between auditors and the preparers of the financial statements was and remains intact. Further, it may also serve as a meaningful reminder to both auditor and auditee the importance of maintaining this independence, which would be an added benefit.
- **Report addressee:** As the auditor by nature serves the company's shareholders and governing body, I think the addressee requirement is reasonable and appropriate, and a necessary addition to the requirements around the audit report. As with the independence statement, I also think it has use as a means of reminding auditors and the companies who employ them that the services provided by the auditor are ultimately acquired at the behest of the shareholders and those charged with governance.
- **Enhancement to the basic elements - financial statement footnotes:** Given how inseparable the notes to the financial statements are from the statements themselves in providing the reader with a complete and accurate portrait of the financial position and results of a company, I wholeheartedly support modifying the language of the audit report to make reference to the notes to the financial statements as being part of the financial statements upon which the auditor is



opining. I hope that it will also encourage and reinforce to the readers that they should spend time reviewing not only the financial statements but also the related footnotes and schedules, thereby enhancing the usefulness of the financial statements taken as a whole.

At the same time, in reading both the initial draft of the proposed rule published in 2013, as well as the reproposal published in May of this year, I concur with multiple other professionals and trade groups that have expressed tremendous concern with regards to the proposal that Critical Audit Matters (“CAMs”) be disclosed within the audit report. My concerns stem from a variety of sources, notably the following:

- I definitively share the belief expressed by many professionals (in many cases via comments provided on the initial draft of the proposal) that the disclosure of such details will prompt an increase in litigation the merits of which prove to be questionable or unfounded. Speaking frankly, I strongly believe that the inclusion of CAMs in the audit report would provide a virtual roadmap for those who may be looking for underhanded ways to enrich themselves via baseless litigation at the expense of a company and/or its auditors.
- I consider it rather likely that the introduction of a new area of complexity requiring significant auditor judgment would result in measurable increases in audit fees, which would ultimately reduce amounts that may otherwise be distributed to shareholders. Additionally, these fees would be attributable not to improved audit quality driven by improvements or increases in audit testing and/or documentation, but rather to an increase in audit firm risk management procedures, involving lengthier reviews by expensive, senior-level individuals both inside and outside of the audit team.
- As the Board knows, the use of professional judgment in the preparation of financial statements—through both the accounting decisions of company personnel, as well as the auditing decisions of those independent accountants whose shareholders they serve—is, by nature, extensive. In addition to the obvious and critical role that researching the correct application of GAAP plays in making important accounting judgments, the ability to openly acknowledge these areas as being more challenging than others, as well as the ability to be transparent in related discussions and share methodology and conclusions with external auditors, is crucial to ensuring the best possible outcomes. I believe this proposal would ultimately inhibit communication with regards to these challenging areas, which in turn would decrease the quality of the accounting and reporting output on these critical issues.
- Simply put, I feel strongly that the inclusion of this highly subjective information in the audit report stands contrary to the factual and objective piece of communication that the audit report is intended to be. Further, to make such a radical change so suddenly (in the sense that the audit report would dramatically change all at once; I acknowledge with appreciation the significant amount of time that the Board has spent crafting this proposal) and without a strong sense of consensus from industry professionals and auditors seems overly ambitious. I appreciate the desire to be transformative in increasing the



utility of the audit report and improving the quality of communications between auditors and shareholders, but I believe a more measured approach—which I think is reflected in many of the other proposals in Docket No. 034, some of which I highlighted earlier—is the correct approach. In addition to the two specific concerns on the CAMs proposal that I mentioned above, I think the potential for unintended consequences and a failure to maximize the effectiveness of the proposal due to a lack of consensus is significant.

Finally, the Board has specifically asked for commentary as to whether or not the disclosure of audit tenure would be more appropriately done through inclusion in the audit report or through submission of Form AP. I would suggest that Form AP would be the most appropriate method of disclosure. As I have detailed previously, the purpose of the audit report—to present an independent auditor’s opinion with regards to the fairness and material accuracy of a specific set of financial statements—seems to indicate that facts about the auditors themselves (e.g. the identity of the signing partner, the tenure of the audit firm with respect to an individual engagement, etc.) are better documented separately from the audit report which appears in a particular set of financial statements. My concern with the inclusion in the audit report arises not from any fear of “overdisclosure”, but rather from the very real possibility that inclusion of these facts in audit reports could (1) shift focus away from the intended subject of the audit report (the accuracy of the financial statements and, for integrated audits, the effectiveness of internal control) and (2) in the absence of context, imply that there is a direct relationship between audit quality and the length of an auditor’s tenure, for which I do not believe there is any compelling evidence.

Thank you again for your consideration of this matter and the opportunity to provide commentary.

Sincerely,

Courtney C. Hathaway
Director of Technical Accounting
(513) 824-7115
chathaway@phillipsedison.com