Via email to: jamesgunn@iaasb.org

September 7, 2012

Mr. James Gunn
IAASB Technical Director
International Auditing and Assurance Standards Board
545 Fifth Avenue, 14th Floor
New York, New York, 10017 USA

RE: Improving the Auditor’s Report – Invitation to Comment

Dear Mr. Gunn:

The Accounting Principles and Auditing Standards Committee ("the Committee" or "We") of the California Society of Certified Public Accountants ("CalCPA") is grateful for the opportunity to comment on the proposed auditing standard referenced above. The Committee is the senior technical committee of CalCPA. CalCPA has approximately 40,000 members. The Committee is comprised of 49 members, of whom 53 percent are from local or regional firms, 27 percent are from large multi-office firms, 10 percent are sole practitioners in public practice, 8 percent are in academia and 2 percent are in an international firm.

Following is a summary of the Committee’s responses to the Invitation to Comment for your consideration.

Overall Considerations

1. Overall, do you believe the IAASB’s suggested improvements sufficiently enhance the relevance and informational value of the auditor’s report, in view of possible impediments (including costs)? Why or why not?

   In general, no. APAS found limited usefulness in a couple of features of the proposal which are discussed in greater detail below, but we think it more likely that the lengthy reports that will be required to meet the proposed changes will actually be more confusing than useful.

2. Are there other alternatives to improve the auditor’s report, or auditor reporting more broadly, that should be further considered by the IAASB, either alone or in coordination with others? Please explain your answer.

   This is hard to answer. Users would like to know the future. This is not attainable with any degree of certainty no matter who is supplying the predictions about the future. To think that auditors can somehow accurately predict the future is folly.

Auditor Commentary

3. Do you believe the concept of Auditor Commentary is an appropriate response to the call for auditors to provide more information to users through the auditor’s report? Why or why not? (See paragraphs 35–64.)

   No. APAS believes that much of the information displayed in the example may be useful to some financial statement readers. APAS believes that changes in the disclosure of information about the
audit client should flow from the Financial Reporting Framework (FRF). To the extent that additional information comes from the FRF then it would be subject to auditing procedures. The APAS believes that, at present, the driving force behind more robust disclosures should come from management who are in the best position to comment on such matters, or the financial accounting standard setters based on established needs of financial statement users. To the extent the FRF is changed, any modifications in the form or content of required disclosures would be established at that time.

The IAASB proposal that auditors prioritize the significance of these disclosures is incomprehensible to us. Is the auditor really to be expected to identify the “really important” disclosures thus relegating the remaining disclosures to the status of not really important?

4. Do you agree that the matters to be addressed in Auditor Commentary should be left to the judgment of the auditor, with guidance in the standards to inform the auditor’s judgment? Why or why not? If not, what do you believe should be done to further facilitate the auditor’s decision-making process in selecting the matters to include in Auditor Commentary?1 (See paragraphs 43–50.)

The APAS believes that the existing ISA 706, Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor’s Report provide enough discretion and guidance. No further auditing standards are needed. Please refer to our answer to the prior question for our views of the role of the FRF on this topic.

Those who would like to have auditors provide commentary operate from the benefit of hindsight. They can tell you with great authority based on events occurring after the issuance of the auditor’s report what they would like to have read in the auditor’s report. However, they can’t tell you what to include looking forward, because no one can see the future.

Also, what happened to the concept of confidentiality of client data? Is there any concern that some of these reporting requirements would require the auditor to violate client confidentiality rules? There should be.

It’s not a question of leaving it to auditor judgment, or trying to come up with more detailed guidance; there should be no auditor commentary.

Re ¶43, if users want to know what auditors discuss with TCWG, why not require TCWG to provide a report?

Re ¶47, it is our belief that requirements such as these will cause many auditors to get out of the business of auditing any financial statements for which this new auditor report is required.

Re ¶48, yes the commentary will need to vary from entity to entity, but “users” is not a monolith. “Users” will rate the significance of different matters differently. Which users’ minds is the auditor to be expected to read?

Re ¶59, requiring the auditor to discuss audit procedures performed will result in reports of interminable length, provide fraudsters a roadmap for how to circumvent the auditor’s procedures and provide fertile ground for an unlimited amount of second-guessing of what the auditor did or didn’t do. What does the IAASB expect to be the benefit to users of such disclosures? Perhaps to assist users in deciding whether or not to rely on the auditor’s report on the financial statements? This will not enhance audit quality, but it will undermine confidence in the auditor’s opinion.
Re ¶62 – The IAASB notes significant impediments, but only discusses its view about costs. What about the other impediments? They are valid reasons for not requiring an auditor commentary. And, as regards costs, it should be noted that the users do not pay for the auditor’s work. If a user wants the auditor’s views about such matters, perhaps a more appropriate track to pursue would be a special agreed-upon procedures engagement at the expense of the user desiring the report.

5. Do the illustrative examples of Auditor Commentary have the informational or decision-making value users seek? Why or why not? If not, what aspects are not valuable, or what is missing? Specifically, what are your views about including a description of audit procedures and related results in Auditor Commentary? (See paragraphs 58–61.)

Given our responses to questions 4 and 5, this question would be not applicable.

The IAASB indicated in the ITC that it is primarily interested in the views of users, but the views of auditors should also be of interest. The proposed description of audit procedures and related results is a quagmire that will lead to auditor’s reports of unimaginable length and detail without any benefit to users other than providing a basis for second guessing and litigation.

6. What are the implications for the financial reporting process of including Auditor Commentary in the auditor’s report, including implications for the roles of management and those charged with governance (TCWG), the timing of financial statements, and costs? (See paragraphs 38 and 62–64.)

The APAS found the particular example of the financial reporting process to be boilerplate in scope—that is, the particular comment could be written for any company in this situation. To the extent that the financial reporting process commentary touched on information about the audit client, it is the view of APAS (as previously expressed) that the driving force behind this information comes from management or the FRF standard setters. To the extent that the financial reporting process commentary calls for information concerning audit strategy, the APAS believes that this information is irrelevant and subject to being misunderstood by the reader—the APAS believes that a general discussion of the role of the auditor is appropriate but that, with the exception of scope limitations, specific discussions of audit strategy may undermine the audit process or improperly imply higher or lower degrees of assurance.

7. Do you agree that providing Auditor Commentary for certain audits (e.g., audits of public interest entities (PIEs)), and leaving its inclusion to the discretion of the auditor for other audits is appropriate? Why or why not? If not, what other criteria might be used for determining the audits for which Auditor Commentary should be provided? (See paragraphs 51–56.)

As stated in our prior answers, the driving force behind additional disclosure of the client should come from management and the FRF standard setters. APAS believes that the guidance in ISA 706 is sufficient to provide guidance to the auditor for additional matters covered in the auditor’s report. APAS also believes that to the extent additional information should be covered in the audit report of PIEs this should be the responsibility of the particular national, or international regulatory oversight agency and not the IAASB.

Going Concern/Other Information

8. What are your views on the value and impediments of the suggested auditor statements related to going concern, which address the appropriateness of management’s use of the going concern
assumption and whether material uncertainties have been identified? Do you believe these statements provide useful information and are appropriate? Why or why not? (See paragraphs 24–34.)

The matter of disclosures of going concern regardless of conditions that raise doubt should be determined by management or FRF standard settler. The IAAGD should not establish standards for disclosure of financial statement assertions. To the extent that such representation is included in the financial statements then it would be appropriately covered by the auditor’s report.

9. What are your views on the value and impediments of including additional information in the auditor’s report about the auditor’s judgments and processes to support the auditor’s statement that no material uncertainties have been identified? (See paragraphs 30–31.)

We think the existing requirements to disclose mitigating factors when there are going concern issues is sufficient. There are always significant risks. Every business is a moment away from being out of business. All that has to happen is the death of key personnel, a natural disaster that wipes out productive capacity, an act of war, the invention of the next generation product that instantly makes the older generation obsolete, etc.

10. What are your views on the value and impediments of the suggested auditor statement in relation to other information? (See paragraphs 65–71.)

The APAS believes that this area is worth exploring. Under ISA 720 the auditor has certain responsibilities with the objective to respond appropriately when documents containing audited financial statements and the auditor’s report thereon include other information that could conflict with, or undermine the credibility of the financial statements and the auditor’s report.

However, it is not practical for the auditor to be assured that s/he has read all such other information that may be in existence. Therefore the APAS believes that it worth studying the implications of specifically identifying in the auditor’s report the other information, if any, that the auditor has read prior to the release of the auditor report.

If this matter is considered further, the APAS believes that it is appropriate to consider whether it is ever possible to specifically identify the “other information” that the auditor has identified as having read in its audit report – there may be different versions of the other information with the same, or similar, name.

Clarifications and Transparency

11. Do you believe the enhanced descriptions of the responsibilities of management, TCWG, and the auditor in the illustrative auditor’s report are helpful to users’ understanding of the nature and scope of an audit? Why or why not? Do you have suggestions for other improvements to the description of the auditor’s responsibilities? (See paragraphs 81–86.)

The APAS believes that it may be worthwhile exploring expanding the description of management’s responsibilities to TCWG as well.
However, our fundamental belief is that this is all irrelevant except maybe to lawyers. Users look back in time to complain about not being sufficiently informed. They will blame anyone they can; the distinction between management’s responsibilities and the auditor’s will ultimately be determined in a court of law.

12. What are your views on the value and impediments of disclosing the name of the engagement partner? (See paragraphs 72–73.)

The APAS is not aware of any value of disclosing the name of the engagement partner, and believe that such disclosure may be confusing. The legal entity standing behind the auditor’s report is the firm regardless of the particular partner.

13. What are your views on the value and impediments of the suggested disclosure regarding the involvement of other auditors? Do you believe that such a disclosure should be included in all relevant circumstances, or left to the auditor’s judgment as part of Auditor Commentary? (See paragraphs 77–80.)

What is the imagined benefit of such disclosure? In our global marketplace, the largest companies have operations in scores of countries, meaning there is involvement of scores of audit firms. The group auditor has the overall responsibility of pulling it all together. Is the goal to undermine user confidence in the group auditor’s report if the user doesn’t care for some component auditor(s)?

14. What are your views on explicitly allowing the standardized material describing the auditor’s responsibilities to be relocated to a website of the appropriate authority, or to an appendix to the auditor’s report? (See paragraphs 83–84.)

This proposal did not receive substantial support of the APAS. Many believed that if the standardized material is getting so voluminous that it is necessary to relocate to a website, that it is time to revisit what is standardized with a goal to reduce the obvious information overload.

The auditor’s responsibilities are detailed in the audit standards which are available to the public from any number of sources. There is no need or benefit to including in every auditor’s report a full or partial regurgitation of these responsibilities. To facilitate this objective, the IAASB, and all regulators that publish auditing standards, should make all auditing standards available on the Internet free of charge to any interested party.

Form and Structure

15. What are your views on whether the IAASB’s suggested structure of the illustrative report, including placement of the auditor’s opinion and the Auditor Commentary section towards the beginning of the report, gives appropriate emphasis to matters of most importance to users? (See paragraphs 17–20.)

The APAS agrees that placing the opinion towards the beginning is a proposal worth considering as many believed that this important piece of information is foremost in the minds of the reader. As discussed in our responses to Questions 3 and 4 above, the APAS does not support the development of an Auditor Commentary section.
16. What are your views regarding the need for global consistency in auditors’ reports when ISAs, or national auditing standards that incorporate or are otherwise based on ISAs, are used? (See paragraphs 21–23 and 87–90.)

The APAS believes that this is a good goal, but believes that each national organization will adopt auditing standards responsive to local regulatory needs, with the goal of international convergence taking second place.

17. What are your views as to whether the IAASB should mandate the ordering of items in a manner similar to that shown in the illustrative report, unless law or regulation require otherwise? Would this provide sufficient flexibility to accommodate national reporting requirements or practices? (See paragraph 17 and Appendix 4.)

The APAS believes that the elements should be mandated, but not the order.

18. In your view, are the IAASB’s suggested improvements appropriate for entities of all sizes and in both the public and private sectors? What considerations specific to audits of small- and medium-sized entities (SMEs) and public sector entities should the IAASB further take into account in approaching its standard-setting proposals? (See paragraphs 91–95.)

Absolutely not. The APAS believes that the current model of general standards with additional guidance, as appropriate, for audits of smaller less complex entities is effective. The proposed requirements are not appropriate for any entities, let alone smaller not listed companies. The IAASB acknowledged in its introductory remarks that this proposal was driven by the input of institutional investors. Why extend these requirements that are onerous and of questionable value beyond the minimum scope necessary to assuage the desires of the institutional investors?

We thank you for the opportunity to comment on this matter. We would be glad to discuss our comments with you further should you have any questions or require additional information.

Sincerely,

Howard Sibel
Chair
Accounting Principles and Auditing Standards Committee
California Society of Public Accountants