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November 22, 2013

Professor Arnold Schilder,
Chairman
International Auditing and Assurance Standards Board (IAASB)
International Federation of Accountants
529 5th Avenue, 6th Floor
New York, New York 10017

Re: Exposure Draft, Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing (ISAs)

Dear Professor Schilder:

CohnReznick appreciates the opportunity to comment on the exposure draft (ED), Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing (ISAs).

CohnReznick is the 11th largest accounting firm in the U.S., with its origins dating back to 1919. We are committed to serving clients that access the capital markets and we recognize the significant role we have in facilitating efficient capital formation. We support the Board's overall objective to improve the value that the audit and the auditor's report contribute to the financial reporting process by providing more relevant information to all stakeholders in the financial reporting supply chain. While our domestic and international capabilities (through our Nexia International membership) allow us to serve a broad array of clients, we are a significant provider of services to the smaller and middle market. Our desire is that our response to the exposure draft will give you perspective into the unique impact these changes might have on small and medium size entities and their ability to attract capital.

Our responses to specific questions on which the Board is seeking comment are included in the attachment to this letter.

If you have any questions concerning our comments or would like to discuss any of our responses or recommendations in more detail, please feel free to contact Kurtis Wolff at 770-330-1167.

Yours truly,

CohnReznick LLP

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**Summary**

We support providing useful information based on the audit performed, and, in particular, the auditor's judgment as to the significant risks to financial reporting for the entity. We support the linkage between what is communicated in the audit report and what is communicated to those charged with governance, and to areas in which the auditor devoted significant attention. We support changes to the overall form and content of the report where those changes clarify the responsibilities of management and the auditor, clarify the meaning of independence, and clarify the limitations of the audit.

In responding to the questions asked in the exposure draft, we have provided for your consideration reasons to alter the proposed requirements for the identification and communication of key audit matters. We also would like to communicate our view that providing the name of the audit engagement partner has not shown to improve audit quality in places where the practice is implemented, and our view is that such information should not be included in the audit report.

We agree with the approach the IAASB has taken in making the proposed ISAs principles-based and flexible enough to be implemented in a manner proportionate with the size and complexity of the entity. However, we also believe there is an inverse relationship between the size of the entity and the frequency with which key audit matters will be described under the proposed requirements. We believe this will lead to smaller and medium size entities bearing a disproportionate share of the cost of implementing the proposed ISA 701.

More detailed reasons for our viewpoints are included in the responses to specific questions below.

**Question 1:** *Do users of the audited financial statements believe that the introduction of a new section in the auditor's report describing the matters the auditor determined to be of most significance in the audit will enhance the usefulness of the auditor's report? If not, why?*

We understand that the introduction of the new section is intended to address the call for the auditor's report to be more informative and for the auditors to provide more relevant information to users based on the audit that was performed. We believe that the introduction of a new section in the auditor's report that describes the significant risks to financial reporting and the areas in which the auditor devoted significant attention or required significant auditor judgment may enhance the usefulness of the auditor's report.

However, we believe including a description of specific audit procedures performed for each key audit matter will not enhance the usefulness of the auditor's report. Such a description may in fact confuse users who are not familiar with the selection and application of audit procedures. We considered a number of examples of items that could technically be under the criteria described in the proposed ISA, but would not ultimately provide insight beyond the pass/fail objective of the report. For example, describing audit procedures performed specifically to address an increased risk of fraud for an account balance has the potential to cause a reader without an audit background to conclude fraud is likely occurring. For a small or medium size entity, auditing a particular area may require proportionally greater effort through specific procedures than for a larger entity, but such information is not necessarily relevant or useful to a user. We believe that the auditor should not be required to make highly subjective judgments in assessing the usefulness of information provided through the key audit matters, which would ultimately result in diversity in practice, further hindering the objective of the ISA.

Our perspective is that the objectives and requirements for identification and communication of key audit matters should align with the type of information that has demonstrable value to the users, and should avoid adding information to the report that either would be of no interest or that might lead to confusion without experienced understanding of auditing. We would refer you to comments made on October 15, 2013, by Mary Jo White, Chairwoman of the Securities and Exchange Commission:

> *"When disclosure gets to be "too much" or strays from its core purpose, it could lead to what some have called "information overload" – a phenomenon in which ever-increasing amounts of disclosure make it difficult for an investor to wade through the volume of information she receives to ferret out the information that is most relevant."*

We believe another approach to providing more value from the audit would be to have those charged with governance provide in their own disclosure more insight stemming from the communications with the auditor. Such an approach would preserve the distinction in the roles around reporting of information between the entity and the auditor. We are concerned that there is the potential for the auditor to report original information about the company, which management has not shared, and that this will cause readers to look to the auditors for incremental information. The practice will further blur the roles between those charged with governance and the auditor. We believe that would be counter to the underlying premise of the objectivity of the independent auditor. Recently, a group of nationally recognized U.S. corporate governance and policy organizations known as the Audit Committee Collaboration, released *Enhancing the Audit Committee Report, A Call to Action*. The document emphasizes the opportunity that audit committees have in reporting on significant matters discussed with the auditor as part of the audit, indicating:

> *"The audit committee should also consider whether additional disclosure about its general oversight of the external auditor – either through descriptions of processes or specific activities – would provide shareholders and potential investors with useful context. These might include discussions of the degree of the audit committee's interaction with the external auditor (including the nature or number of meetings outside the presence of management), the types of issues discussed at those meetings, and other activities that are central to the audit committee's oversight."*

**Question 2:** *Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide an appropriate framework to guide the auditor's judgment in determining the key audit matters? If not, why? Do respondents believe the application of proposed ISA 701 will result in reasonably consistent auditor judgments about what matters are determined to be the key audit matters? If not, why?*

We believe that communication in the auditor's report of those areas where the auditor encountered significant difficulty, including with respect to obtaining sufficient appropriate audit evidence, or significant modifications to the planned approach to the audit, including as a result of the identification of a significant deficiency in internal control, will not enhance the user's understanding of the entity being audited. Communication of such matters may be inferred by the users of the financial statements as a separation of the audit opinion into matters in which the auditor is more and less confident. The information communicated in the auditor's report should be reported in a manner which does not cast doubt on whether the audit was performed satisfactorily. The current auditor reporting model has always reflected a high standard of not implying piecemeal opinions (in fact such opinions are prohibited). Disclosing information regarding how difficult it was to achieve that standard could be viewed by users incorrectly as a qualification of whether that standard was achieved. Consequently, users could perceive an audit with reported difficulties as being indicative of a lower quality audit than an audit without reported difficulties. Such a perception would be misleading and could actually damage the entity being audited if a communicated audit difficulty is viewed by users as a perceived risk regarding the company.

Additionally, because “significant difficulty” is a subjective description, we are concerned such communications could lead to inconsistency about what matters are determined to be the key audit matters.

Management is not always required to disclose significant deficiencies, and we believe it is not appropriate to disclose in key audit matters something management would otherwise not disclose in the course of their reporting. This view is consistent with the guidance in paragraph A37 of the proposed ISA, which indicates that it is appropriate for the auditor to seek to avoid providing original information about the entity.

We believe that the proposed requirement to describe the areas identified as significant risks in accordance with ISA 315 or involving significant auditor judgment is appropriate, and will result in reasonably consistent auditor judgments. It is reasonable for a user of the financial statements to understand that certain risks to financial reporting are more significant for a particular entity, or require greater auditor judgment, and we do not believe such an understanding leads to diminished confidence in the audit report.

**Question 3:** *Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide sufficient direction to enable the auditor to appropriately consider what should be included in the descriptions of individual key audit matters to be communicated in the auditor’s report? If not, why?*

In the context of our response to Question 2 above, we believe that the related application material in proposed ISA 701 provides sufficient direction to enable the auditor to appropriately consider what should be included in the descriptions of individual key audit matters. However, we do not believe it is appropriate to provide descriptions of specific audit procedures, as suggested by the examples of key audit matters in the illustrative audit report. We believe our view is consistent with paragraph A30 of the proposed ISA, which indicates the auditor should limit the use of highly technical auditing terms that would be confusing to users who do not have a reasonable knowledge of auditing.

Further to the consideration points provided in our response to Question 1 above, we are concerned that communication of specific auditing procedures or responses to significant risks will lead to further inconsistencies in reporting and user confusion. Auditors can respond to similar significant risks in various ways. Such responses can be influenced by matters that users may not understand, such as auditor or firm policies and preferences. Ultimately, the auditor is charged with responding to significant audit risks as necessary to reduce the risk of material misstatement to an appropriately low level. How the auditor accomplishes that objective can vary and communicating such information does not enhance the user's understanding of the entity being audited. Additionally, firms that focus on a given industry likely have developed proprietary approaches to auditing critical risk areas. Describing those procedures outside the context of the audit as a whole could be confusing even to those within the profession. A desire to protect such proprietary approaches would likely lead to "boiler plate" responses adding length, but no value, to the auditor's report.

**Question 4:** *Which of the illustrative examples of key audit matters, or features of them, did respondents find most useful or informative, and why? Which examples, or features of them, were seen as less useful or lacking in informational value, and why? Respondents are invited to provide any additional feedback on the usefulness of the individual examples of key audit matters, including areas for improvement.*

Consistent with our response to Question 3 above, our view is that the description of specific audit procedures similar to those in the illustrative examples for Revenue Recognition Relating to Long-Term Contracts and Valuation of Financial Instruments should be avoided. We found the illustrative key audit matter examples of Acquisition of XYZ Business and Goodwill to be more in line with our view of how the key audit matters should be communicated, as the primary focus of the text was to communicate why these matters were significant risks or involved significant auditor judgment.

**Questions 5-8, and 13-14:** Our responses to other questions in the proposal or in our summary above address some of the issues arising from these questions. We have opted not to provide additional written responses to them.

**Question 9:** *Do respondents agree with the statements included in the illustrative auditor's reports relating to:*

*(a) The appropriateness of management's use of the going concern basis of accounting in the preparation of the entity's financial statements?*

*(b) Whether the auditor has identified a material uncertainty that may cast significant doubt on the entity's ability to concern, including when such an uncertainty has been identified (see the Appendix of proposed ISA 570 (Revised)?*

*In this regard, the IAASB is particularly interested in views as to whether such reporting, and the potential implications thereof, will be misunderstood or misinterpreted by users of the financial statements.*

We believe that providing the expanded explanation of the going concern basis of accounting and an indication of management's identification of any material uncertainty may diminish the primary intent of the paragraph, which is to communicate to the reader when there is substantial doubt about an entity's ability to continue as a going concern.

**Question 12:** *What are respondents' views as to the proposal to require disclosure of the name of the engagement partner for audits of financial statements of listed entities and include a "harm's way exemption"? What difficulties, if any, may arise at the national level as a result of this requirement?*

We do not believe that disclosure of the name of the engagement partner improves audit quality, and our view is that inclusion of the engagement partner's name in the audit report creates unnecessary harmful consequences for the person named, regardless of the outcome of the audit.

**Scalability:** The Board also sought feedback on the IAASB's view that the Proposed ISAs can be implemented in a manner proportionate to the size and complexity of an entity, and on areas where additional guidance may be helpful to illustrate how the Proposed ISAs can be implemented in a proportionate manner.

We believe the proposed ISAs need to be able to be implemented in a manner proportionate to the size and complexity of an entity in order to be viable. However, we are concerned that objective may not be achieved in the proposal's current form. Specifically, we believe that communication in the auditor's report of any matters other than those accounts and disclosures which embody significant inherent risks will result in significant differences in the communications made in connection with audits of smaller entities and that such additional communications will not only increase the costs associated with such communications, but also could put such smaller entities at a competitive disadvantage in attracting capital.

We believe that the objective of auditor communications should be to communicate on a consistent basis those areas of the audit which reflect higher inherent risk. Communication of other matters, such as additional procedures performed because of internal control deficiencies, issues of management competency, or identification of fraud risks will create differences and inconsistencies in reporting by auditors and will focus more attention on the audit process than on the results of that process. In other words, communications by auditors should contain similar information for similar entities. We believe that this can only be achieved by limiting the matters to be communicated to inherent risks related to significant accounts and disclosures.

Requiring disclosures related to increased audit difficulties resulting from other issues, such as internal controls, mistakes, talent or competency levels of management, or the quality of oversight provided by those charged with governance would almost certainly result in some increased adverse impacts on smaller entities. The result is that these smaller entities would likely suffer increased audit costs and could suffer competitive disadvantages because of a market perception that they were riskier or more difficult to audit. Also, as significant audit matters will be handled by the most experienced members of the audit firm and the more senior members of those charged with governance, they will generally consume the time of the most costly resources. In a smaller engagement team and smaller company environment, those resources are less likely to be able to leverage their time to other members of either of those parties. Therefore, the smaller environment will disproportionately bear the greater burden of the costs of this additional reporting. For this and many other reasons, The Securities and Exchange Commission – Advisory Committee on Small and Emerging Companies, in their report to the Commission's Chairman dated March 21, 2013, specifically recommended that smaller reporting companies should be exempted from such additional auditor reporting requirements.

Finally, we are also concerned that reporting by auditors of areas where application of extended auditing procedures was required as a result of perceived deficiencies in internal controls could cause smaller entities to feel increased pressure to eliminate such issues. Many smaller entities may not be able to afford more robust internal control systems, and such systems would not be warranted to accomplish reliable and transparent financial reporting, but rather would only be implemented in order to avoid emphasis of an area in the auditor's report. Such would be a costly unintended consequence of these proposed requirements. Likewise, requiring smaller entities to adopt and report on the effectiveness of their internal control systems was hotly debated in connection with implementation of section 404b of Sarbanes-Oxley. Ultimately, the requirement that auditors report on the effectiveness of the internal control systems of smaller entities under section 404b of Sarbanes-Oxley was not implemented. Such issues should not be reopened through the auditor's communication of audit difficulties. We believe companies should benefit from the lessons learned in placing such non-scalable reporting requirements on the smaller and medium sized entities, and the negative consequences and confusion that event created for all financial reporting stakeholders.