

November 5, 2003

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 009, *Proposed Rule Regarding Certain Terms Used in Auditing and Related Professional Practice Standards*

Dear Board Members and Staff,

We appreciate the opportunity to comment on the Public Company Accounting Oversight Board's ("Board" or "PCAOB") proposed Rule 3101 regarding certain terms to be used in the Auditing and Related Professional Practice Standards to describe the differing levels of professional obligations to be imposed on registered public accounting firms and their associated persons ("auditors").

We support the Board's intentions and actions to improve audit quality and believe that the imperatives identified by the Board are primarily consistent with the way auditors currently interpret and apply generally accepted auditing standards (GAAS) adopted by the Auditing Standards Board of the American Institute of Certified Public Accountants. We do, however, have concerns with respect to the proposal and certain other related matters, as follows.

Contemporaneous Documentary Evidence

The Board has proposed to use the term "should" to indicate obligations that are presumptively mandatory and ordinarily must be performed by the auditor. Alternative actions with respect to such obligations must be justified by verifiable, objective and documented evidence, contemporaneous with the audit. We agree with the use of the term "should" to indicate a high threshold of obligation consistent with the current interpretation of existing standards. However, we believe that the contemporaneous documentation requirement (in effect documenting what was not done) will not increase the quality of audits but rather add tremendous cost to an audit.

The nature, timing and extent of audit procedures and the quantity, type and content of audit documentation are matters involving the professional judgment of the auditor. Many factors are considered in determining the nature, timing and extent of audit procedures and the quantity, type and content of the documentation for a particular audit area, such as the risk of material

misstatement, significance of the account or class of transactions, relevance of the assertions, extent of judgment involved in performing the work and evaluating the results, nature of the procedure, nature and extent of exceptions identified, and the significance of evidence obtained. Certain conclusions are readily determinable from the work performed or are evident from a review of the financial statements (e.g., immaterial account balance). The auditor, therefore, considers the need to document a conclusion or the basis for a conclusion that is not otherwise readily determinable.

In lieu of the proposed requirement, we recommend that the rule require the auditor to consider the significance of the particular audit area to which the “should” directive relates. For audit findings or issues that are significant, the auditor should document the actions taken, any additional evidence obtained, and the basis for the final conclusions reached. This requirement is consistent with existing standards and allows auditor judgment in determining the nature and extent of audit documentation. Such requirement also reduces the time and effort required to document procedures relating to insignificant matters or matters that are readily determinable from the existing documentation.

Use of Terminology in Interim Board Standards

The Board’s Interim Professional Auditing Standards were adopted on an initial, transitional basis until the Board could determine whether such standards were appropriate to adopt permanently. The Board stated that it would establish a schedule and procedures to review such pre-existing standards, on a standard-by-standard basis, to determine whether they should be permanent, repealed, or modified.

The Board has now proposed to extend the differing levels of professional obligations as described in the proposed rule to the interim standards. Such pre-existing standards were drafted under a separate framework that required a high threshold of obligation by using the words “is required” and “should,” but allowed the auditor to justify a departure using persuasive and/or documented evidence. Accordingly, we believe that the term “should” in the interim standards implies an obligation that is presumptively mandatory, and in certain circumstances, an obligation that is unconditional. We do not believe that the lack of performance of a “should” directive, however, constitutes a “failure” under existing standards, as indicated by the Board.

Notwithstanding our concerns expressed above, we oppose the application of the contemporaneous documentation requirement to the interim standards, without actually performing a standard-by-standard review to determine the impact of such a request. Although we support the Board’s intentions, we believe this obligation may lead to an unintended result, simply due to the framework used to draft the interim standards.

For example, footnote two states “Therefore, if a Board standard provides that an action or procedure is one that the auditor “should consider,” consideration of the action or procedure is presumptively mandatory, while the action or procedure is not.” We believe that in certain circumstances, under the interim standards, the action or procedure itself is presumptively mandatory. For instance, paragraph 34 of SAS No. 99 (AU Section 316), *Consideration of Fraud in a Financial Statement Audit*, states the following:

“The auditor should consider other information that may be helpful in identifying risks of material misstatement due to fraud. Specifically, the discussion among the engagement team members (see paragraphs 14 through 18) may provide information helpful in identifying such risks. In addition, the auditor should consider whether information from the results of (a) procedures relating to the acceptance and continuance of clients and engagements¹⁴ and (b) reviews of interim financial

statements may be relevant in the identification of such risks. Finally, as part of the consideration of audit risk at the individual account balance or class of transaction level (see SAS No. 47, AU sec. 312.24 through 312.33), the auditor should consider whether identified inherent risks would provide useful information in identifying the risks of material misstatement due to fraud (see paragraph 39).”

In this circumstance, the word “consider” is used to define something the auditor is required to think about when identifying risks of material misstatement due to fraud. This paragraph does not infer that the auditor has the option of not performing such procedures, after they have considered them. Accordingly, the action or procedure itself is presumptively mandatory.

Scope of Proposed Rule 3101

The Board’s adoption of interim standards incorporated the content of the existing body of literature, including auditing standards, interpretive publications, and other auditing publications. An auditor is required to comply with the auditing standards. An auditor should also be aware of and consider interpretive publications applicable to the audit. If the auditor does not apply the auditing guidance included in an applicable interpretive publication, the auditor should be prepared to explain how he or she complied with the auditing standards addressed by such guidance. When using other auditing publications, the auditor should be satisfied that, in his or her judgment, it is both relevant to the circumstances of the audit and appropriate.

We are aware of several instances where the interpretive publications (“level 2” GAAS) and other auditing publications (“level 3” GAAS) utilize the terms proposed by the Board to describe professional obligations. Proposed Rule 3101 does not directly address the application of the differing levels of obligations to the interpretive and other auditing publications. Accordingly, we recommend that the Board clarify how the differing levels of professional obligations relate to level 2 and level 3 GAAS.

Other Descriptive Material

The proposal contains descriptive material, such as background information and reasons and conclusions reached. It also includes an analysis by section in Appendix 2. Such material is not included in the proposed rule, but appears to be included to assist registered public accounting firms and their associated persons in understanding and implementing the rule. We recommend that the PCAOB clarify the authoritative status of such information and describe how it will be maintained for reference purposes.

Exposure Period


We acknowledge and support the PCAOB’s authority to establish and adopt auditing, quality control, ethics, independence and other standards relating to the preparation of audit reports for issuers. However, we also promote the development of global generally accepted standards, which we believe will lay the foundation for consistent, timely, reliable and transparent information in global financial markets. The Public Oversight Board’s Panel on Audit Effectiveness also noted the development of a uniform global set of standards as part of its findings.

Hence, we believe it is essential and in the public interest for the rulemaking process to allow sufficient time for interested parties around the globe to submit comments. We recommend that the Board recognize and consider any comments received from international organizations subsequent to the date the comment period for this docket matter ends. Such interested parties may not have been provided with adequate time to submit written comments, as many countries

would need to first translate the document. We urge the Board to consider such matters for future proposals.

We would be pleased to discuss any of our comments with you. If you have any questions, please contact Mr. John L. Archambault, Managing Partner of Professional Standards, at (312) 602-8701.

Very truly yours,

A handwritten signature in black ink, reading "John L. Archambault". The signature is written in a cursive style with a large initial "J" and "A".

Grant Thornton LLP