

Düsseldorf, November 6, 2003

Public Company Accounting Oversight Board  
(PCAOB)  
Office of the Secretary  
1666 K Street, N.W.,  
Washington, D.C.  
20006-2803  
  
USA

By E-Mail: [comments@pcaobus.org](mailto:comments@pcaobus.org)

Dear Sir(s):

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

We would like to thank you for the opportunity to comment on the PCAOB Proposed Rule Regarding Certain Terms Used in Auditing and Related Professional Practice Standards. The Institut der Wirtschaftsprüfer represents approximately 85 % of the German Wirtschaftsprüfer (German Public Auditor) profession. The German profession seeks to comment on the proposals by the PCAOB noted above because we believe that this Proposed Rule will affect not only the development of auditing standards in the United States, but also influence auditing standards on a worldwide basis. Furthermore, a significant number of German Wirtschaftsprüfer are or will be subject to the requirements of the Sarbanes-Oxley Act.

**General comments**

We were disappointed to see the very short exposure period in which comments can be provided to the PCAOB. Comment periods of 30 days are too short in an international environment, since many organizations would like to have the opportunity to consult with their stakeholders. We would suggest that 60 days might be more appropriate for short proposals such as this one; 90 days may be adequate for longer proposals.

We support the establishment of a sound basis for setting and interpreting auditing and related professional practice standards (hereinafter, we will refer only to auditing standards, but mean both auditing and related professional practice standards). In our view, the establishment of such a sound basis is predicated upon the development and application of rigorous definitions of terms used in auditing standards. Consequently, we support the efforts of the PCAOB to bring clarity into its auditing standard setting processes and the interpretation of these standards.

However, we suspect that terms in relation to the degree to which the PCAOB expects registered public accounting firms and their associated persons to comply with the professional obligations included in those standards do not constitute the only terms that may require definition. We therefore believe that the PCAOB rules constituting auditing standards ought to include a section on definitions, much like the Glossary of the International Standards on Auditing, that covers the key terms used in the standards. In addition, it may be helpful to readers seeking to interpret the standards if the rules also included a section that covered the major drafting conventions covering the use of language (and the reasons for using a particular convention) in setting the standards.

## **Comments on Rule 3101 by Paragraph**

### *Unconditional Obligations*

Rule 3101 (a) (1) proposes that the words “must”, “shall”, and “is required” indicate unconditional obligations that the auditor must accomplish in all cases in which the circumstances exist to which the obligation applies. We would like to point out that the phrase “in all cases in which the circumstances exist to which the obligation applies” makes the obligation conditional upon the existence of certain circumstances. In our view, this implies that words or phrases indicating unconditional obligations should only be used in conjunction with **circumstances explicitly specified** in the standard that lead to the application of the obligation, because the lack of such specificity of circumstances may lead to the scope of application of the obligation being unclear. This is a good example of a drafting convention that may need to be established in connection with the use of words and phrases that create obligations.

Furthermore, we believe that it is incumbent upon the PCAOB to ensure that unconditional obligations that apply in circumstances explicitly specified in the standard *always* apply – that is, the existence of a single counterexample should be sufficient to prevent the use of wording that indicates an unconditional obligation. Of course, the explicitly specified circumstances could be adjusted to ensure that one or a few coun-

counterexamples are taken into account to allow the application of wording leading to an unconditional obligation, but this implies that no additional counterexamples may exist. On this basis, we surmise that the use of wording leading to unconditional obligations for explicitly specified circumstances will be relatively rare, which is in consonance with the PCAOB's view as expressed in Part A of the Release that such unconditional obligations will be used sparingly.

We would agree that a *clear* failure to discharge an unconditional obligation ought to be a violation of Rule 3100. However, there may be some question as to whether or not the explicitly specified circumstances exist to which the obligation applies, and hence, it may be unclear as to whether failure to discharge has occurred. The questions that arise in this respect is whether the auditor or the PCAOB bears the burden of production that these explicitly specified circumstances did not exist at the time of the audit, and that therefore a violation has occurred, and what burden of persuasion applies. This question ties into our comments on presumptively mandatory obligations (see below).

With respect to the burden of production, we note that under Rule 5204 (a) the interested division of the PCAOB bears the burden of proving that a violation has occurred. Hence, an auditor's failure to prove that no violation has occurred does not in itself entitle the PCAOB to conclude that a violation has occurred. Consequently, if an auditor does not perform an unconditional obligation on the grounds that the explicitly specified circumstances creating the unconditional obligation do not exist in a particular case, the auditor is not required to prove to the PCAOB that these circumstances did not exist: rather, the PCAOB must prove that a violation has occurred because the explicitly specified circumstances did exist. Therefore, it would not be appropriate to place the onus on the auditor to prove that, at the time of the audit, the explicitly specified circumstances did not exist because this would not be consistent with the burden of production stipulated in Rule 5204 (a). Nevertheless, this does not relieve the auditor from the obligation to gather and evaluate evidence concerning the existence of the explicitly specified circumstances and to document the evidence gathered, evaluation performed and conclusions drawn.

A violation of evidence gathering and documentation requirements by the auditor in this respect does not imply that the explicitly specified circumstances did not exist. We recognize, however, that the violation of evidence gathering and documentation requirements by the auditor where the consequent lack of evidence precludes the PCAOB from making a judgment as to whether the explicitly specified circumstances existed then ought to result in disciplinary action commensurate to the violation of an unconditional obligation. This discussion about evidence begs the question as to what evidence and documentation requirements ought to be established for the audi-

tor for those situations in which the auditor decides that the explicitly specified circumstances did not exist. However, it appears that this question can only be answered in relation to the burden of persuasion that the PCAOB must meet to prove that the explicitly specified circumstances existed at the time of the audit.

Rule 5204 (a) states that the interested division of the PCAOB must prove that a violation has occurred by a preponderance of the evidence. In our view, if the Rules require the PCAOB to meet a low burden of persuasion (preponderance of the evidence) to support the existence of explicitly specified circumstances leading to the applicability of an unconditional obligation and a finding of a violation, but require the auditor to meet a higher burden of persuasion (i.e., either clear and convincing evidence or beyond any reasonable doubt) to justify that explicitly specified circumstances do not exist, then this will lead to situations in which the auditor performs procedures because he or she cannot meet the burden of persuasion required, even though the PCAOB would have concluded under a lower burden of persuasion that the auditor need not have performed those procedures. In other words, the auditor would be performing procedures that the PCAOB would have otherwise concluded as not having been necessary. Consequently, we believe that an auditor need only satisfy himself or herself by the preponderance of the evidence that the explicitly specified circumstances do not exist.

The application of a lower burden of persuasion is, of course, particularly relevant in situations where verifiable, objective evidence may be difficult to obtain. In conclusion, we believe that failure to discharge an unconditional obligation would arise only if the PCAOB proved by a preponderance of the evidence that those explicitly specified circumstances exist to which the obligation applies. Hence, auditors should obtain and document enough evidence to satisfy themselves by a preponderance of that evidence that such circumstances do not exist when they decide that an unconditional obligation is not applicable. An important point in this respect addressed in the proposed rule 3101 (a) (3) but not in (1) is that the decision as to whether a preponderance of the evidence that explicitly specified circumstances leading to an unconditional obligation exist or do not exist has been obtained and properly documented may involve the exercise of considerable professional judgment on the part of the auditor.

As a practical matter, we believe some additional flexibility of wording should be allowed for indicating unconditional obligations so that the language of the standards does not become awkward. Other possible phrases that come to mind include “have to”, “need to”, “requires”, or “entails”. Furthermore, sometimes such obligations can be expressed by the use of adjectives (e.g., “required”, “compulsory”, etc.). In any case, the PCAOB should develop a policy for using the different kinds of wording for unconditional obligations in a consistent manner.

### *Presumptively Mandatory Obligations*

We agree that some obligations should be presumptively mandatory, and that the word “should” can be used to describe these kinds of obligations. However, given our discussion of the burden of production and persuasion that ought to be borne by the auditor in deciding not to apply unconditional obligations, we do not agree with the standard of evidence required of the auditor to overcome the presumption.

We consider the proposed requirement (in which violation of Rule 3100 would occur when an auditor fails to demonstrate, by verifiable, objective, and documented evidence, that alternative actions he or she followed in the circumstances were sufficient to achieve the objectives of the standard and serve adequately to protect the interest of investors and further the preparation of informative, fair and independent audit reports) to place the burden of production upon the auditor, which is not consistent with Rule 5204 (a), and to require the auditor to do so with a burden of persuasion that exceeds that required of the PCAOB (preponderance of the evidence) in that Rule. Furthermore, we do not believe that the auditor should carry the burden of establishing that, in the circumstances, compliance was not necessary to achieve the objectives of the standard.

Like unconditional obligations, presumptively mandatory obligations would need to be defined in conjunction with explicitly specified circumstances (as we defined in our discussion on unconditional obligations) that lead to the presumption. Of course, this means that auditors need to obtain and document enough evidence to satisfy themselves by a preponderance of the evidence that such circumstances do not exist when they decide that a presumptively mandatory obligation is not applicable. As mentioned previously, this may require the auditor to exercise considerable professional judgment.

In a similar manner, if an auditor comes to the conclusion that a presumptively mandatory obligation is applicable based upon the circumstances, we believe that the auditor need only overcome, by obtaining and documenting preponderance of the evidence, the presumption that only the fulfillment of this obligation (as opposed to

some other means) will fulfill the objectives of the engagement (which, presumably involves the protection of the interests of investors *through* the preparation of informative, fair and *objective* audit reports). In this case, the auditor must obtain and document the preponderance of the evidence to satisfy himself or herself that the presumption has been overcome by means other than the presumptively mandatory obligation. This decision and the adequacy of its documentation may also require the exercise of considerable professional judgment by the auditor. A violation of Rule 3100 would, in our view, only occur if the auditor did not fulfill the presumptively mandatory obligation and the PCAOB proved by a preponderance of the evidence that: 1. the explicitly specified circumstances exist to which the presumptively mandatory obligation applies and 2. the objectives of the engagement (as we defined above) had not been fulfilled by other means, or 3. the auditor has not obtained or properly documented adequate evidence to satisfy himself or herself that either the explicitly specified circumstances do not exist or the objectives of the engagement have been fulfilled by other means.

#### *Professional Obligations to Consider*

We also agree that terms such as “may”, “might”, “could” and other terms and phrases be used to describe actions and procedures that auditors have a professional obligation to consider.

#### *Application of the New Terminology to the Interim Standards*

We are concerned that the impact of the new terminology on the interim standards may not have been sufficiently analyzed in detail – sentence by sentence in each paragraph. We believe that giving new meaning to old words in existing standards is a process likely to lead to confusion in the application of standards. We would prefer the PCAOB to apply the new terminology consistently only in any new standards issued by the PCAOB, because this would give those affected by the new standards the opportunity to comment on the impact of those words on their obligations. In essence, applying new meanings to the old standards does not allow those affected to properly assess that impact in the exposure period given, nor to then provide the PCAOB with their comments on those impacts.

We hope you find our comments helpful and would be pleased to be of assistance to you if you have any questions about these comments.

Yours very truly,



Dr. Gross  
Executive Director



Wolfgang P. Böhm  
Referatsleiter

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