The Association for
Accountants and
Financial Professionals
in Business

January 16, 2012

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

Rulemaking Docket No. 29

Dear Members of the Board:

The Financial Reporting Committee (FRC) of the Institute of Management Accountants (IMA) is pleased to comment on the PCAOB's proposed amendments to auditing standards and Form 2 covering disclosure in the audit report and Form 2 of the name of the audit partner and disclosure in the audit report of other firms and persons that took part in the audit.

The FRC is the financial reporting technical committee of the IMA. The FRC includes preparers of financial statements for some of the largest companies, representatives from the largest accounting firms, valuation experts, accounting consultants, academics, and analysts.[1] The FRC reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations.

In general, we support the second part of the proposal: to require disclosure of the name, headquarters location, and measure of involvement of other independent public accounting firms and other persons that took part in the audit. Generally, investors are unaware of this information and its inclusion will improve users' understanding of how auditors conducted the audit.

However, requiring disclosure of the name of the engagement partner would not improve audit quality or provide sufficient other value to audited financial statements. For reasons explained below, we do not favor adopting this requirement. Rather, we are in Board Member Dan Goelzer's camp per his statement at the October 11th public meeting, "In my view, the Board would need more evidence than it has now to conclude that partner identification would improve audit quality."

[1] Additional information about the IMA Financial Reporting Committee can be found at www.imafrc.org.

Suite 1
Montvale, NJ 07645
www.imanet.org

Information about other accounting firms, etc.

An important aspect of this part of the proposal is how it applies to international accounting firms or associations. As we understand the proposal, an international accounting firm performing the audit for a multi-national corporate entity with operations in many parts of the world would have to disclose that parts of the engagement were performed by its affiliated firms in, say, China, England, Argentina, Mexico, and Australia, assuming each met the materiality threshold. While firms with international associations have active quality control programs and may perform similar audit approaches worldwide, they are still separate legal entities and investors may consider that to be important information.

We agree with the statements made by Chairman Doty and Board Member Hanson when announcing the proposal:

Doty

> I am concerned about investor awareness. I have been surprised to encounter many savvy business people and senior policy makers who are unaware of the fact that an audit report that is signed by a large U.S. firm may be based, in large part, on the work of affiliated firms. Such firms are generally completely separate legal entities in other countries.
>
> Enhanced transparency into the composition of cross-border audits should help investors gain a better understanding of how an audit was conducted and make more informed decisions about how to use the audit report.

Hanson

> Moreover, even where the other firm is a member of the international network of the firm issuing the audit report, the network affiliate firm may be subject to different, and potentially conflicting, legal and regulatory requirements that investors may want to consider in evaluating the overall audit.

There is also the question of the lack of PCAOB inspection access to auditors in certain countries, most notably China at present. This disclosure would inform users that a firm's affiliate not subject to PCAOB inspection has performed some portion of the overall audit.

Given these considerations, it is reasonable for the PCAOB to require disclosure of the percentage of audit hours performed by each separate legal entity within the signing firm, subject to a materiality threshold.

Our comments on a few of the questions raised in the proposal follow.

26 **What is the best measure of the extent of other participants' involvement in the audit?** – Almost any measure of the extent of other participants' involvement will be somewhat arbitrary

so the estimated hours seem as reasonable as anything else short of trying to figure out a measure of the relative risks involved, which would not be practical.

27 **What challenges would there be in acquiring other participants' audit hours?** – There are many implementation questions such as: Will the other participants have to provide some sort of certification for their audit hours in order for the signing audit firm to be able to rely on them in making the percentage calculation? Would the signing auditor be able to obtain an interim actual number of hours and then extrapolate it to determine an estimate rather than waiting for a final actual? We think auditors would figure these things out on their own but some guidance in the final release might be helpful.

31 **What should be the minimum threshold for disclosing another auditor's participation?** The 3% threshold strikes us as too low although any number picked will be arbitrary. Based on the example in your Appendix, we suspect that investors would not have a much different impression of the situation if the threshold were 5% rather than 3%. Disclosing three different firms and over 20 percent audited by other firms would still indicate a great deal of spreading of the audit responsibility. About the only thing that might be gained in the case of a lower threshold in this example would be if the 3% and 4% countries were ones where the PCAOB was unable to inspect auditors. However, (1) the proposal does not require disclosure of whether the PCAOB can inspect auditors in the headquarters country or (2) you do not require disclosure of whether the PCAOB has inspected the firm. These factors seem to argue for a somewhat higher threshold and we think 5% would be adequate. Or perhaps there should be required disclosure in all cases when an other than de minimus part of the overall examination has been performed in a country not subject to PCAOB inspection, with a somewhat higher threshold for other countries.

Disclosure of name of engagement partner

As mentioned above, we do not believe that requiring disclosure of the name of the engagement partner in the auditor's report would improve audit quality or provide sufficient other value to audited financial statements.

From the proposal, it appears that the PCAOB is not convinced either. The words "could" and "might" appear often in the section explaining the Board's reasoning for proposing this requirement. For example, "The Board is, by this proposal, considering whether additional transparency about the identity of the person responsible for the engagement could provide investors with useful information and could further incentivize firms to assign more experienced and capable engagement partners to engagements." And, "As discussed above, disclosure of the name of the partner responsible for the audit might increase the partner's sense of accountability and might provide useful transparency."

In fairness, the proposal does quote a few comment letters on the earlier concept release that support the disclosure. However, we believe that in a formal proposal to amend auditing standards, the Board should express more conviction for its position based on the evidence gathered over the six years the project has been under study. If such equivocal language is indicative of Board members' real uncertainty about this matter, it is unclear what you will learn from comments on this draft beyond repeating earlier views.

Some might argue that knowing the engagement partner's name could help investors in cases where the partner was associated with repeated instances of poor reporting practices. However, these situations likely would be rare. Audit committees generally scrutinize partners' qualifications during the rotation process and are reluctant to accept weak or tainted partners. So too, accounting firms' quality control processes closely monitor partner performance for client service, firm reputation and litigation exposure. The vetting process is particularly strong for engagement partners on the largest corporations.

We are also concerned with unintended consequences such as the market unfairly tainting an engagement partner without cause or due to misunderstanding. For example, a restatement for error could occur even though the named partner had overseen acceptable audit work (or relied on the work of another firm where the problem occurred). Or, the market could be confused about which partner presided over restatement for error. This could occur, for example, when a new partner discovers a problem resulting in restatement even though a partner from a previous year's audit (unnamed in the report) might have missed the problem.

The release notes that investors and investor advocates who commented on the concept release generally agreed that a signature requirement would enhance accountability and transparency and, in turn, investor protection. We do not agree the notion that naming an individual would somehow cause greater accountability. When authorizing issuance of audit reports or certifications or sub-certifications of financial reports in the case of corporate accountants, there is already full, personal responsibility for that information. Including individual names in the audit report does not increase the already high burden of responsibility for quality financial reporting and audit work.

We also note that the issuance of the audit report is very much a "team effort." Depending on the size of the reporting company, this can involve anywhere from a few other individuals to hundreds. While the engagement partner plays a very important role in coordinating the overall audit, she or he depends on many others. To name a single individual is to imply that one person accepts responsibility rather than the firm, which we believe is the wrong representation. Thus, we strongly believe the name of the engagement partner should not be a required disclosure.

We note that the European Commission recently proposed a new auditor's report that would include the names of all members of the audit team. That would clearly be overkill but it would at least be more reflective of the team effort that pervades any engagement.

We would be pleased to respond to any questions you have about our comments. You can reach me at 212 664-1733.

Allan Cohen
Chair, Financial Reporting Committee