

Kevin Gomez
1736 Hobart St NW
Washington, DC 20009

November 26, 2013

Public Accounting Oversight Board

RE: PCAOB Rulemaking Docket Matter No. 034; Proposed Rule Under Release No. 2013-005; Release Date August 13, 2013

Comments Related to Critical Audit Matters (Paragraphs 7 – 14 of the Proposed Auditor Reporting Standard)

Members of the Board:

I appreciate the opportunity to respond to the request for comments on *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion* (the "Proposed Standard"). I am electing to limit my comments to this Proposed Standard, and I specifically wish to address selected questions concerning Critical Audit Matters. I write as a member of the financial community and a potential investor.

Overview

In general, I agree with the spirit and intent of the Proposed Standard. While the current form of the auditor's report gives boilerplate language regarding the auditor's procedures, there is a general understanding that in the course of their procedures certain matters may have warranted significant effort in order to gain comfort. The auditor is in a unique position to provide further detail regarding areas of significant judgment or risk that their own procedures identified as requiring additional attention. The investing community would certainly benefit from having this insight, as the current pass/fail model of the auditor's report gives no specifics as to the particular issues of concern for a company. There are several examples of public companies that have experienced financial scandals and subsequent restatements while having previously received an unqualified opinion from their auditor. While I am sure that such auditors did indeed perform sufficient procedures as to obtain reasonable assurance regarding the presentation of the financial statements, I cannot help but wonder whether insight regarding risky areas might have given the investing community at the very least some indication to tread lightly where there may have been aggressive accounting treatment or management estimation.

The following comments are in response to certain questions set forth in the Proposed Standards.

10. Would the auditor's communication of critical audit matters be relevant and useful to investors and other financial statement users? If not, what other alternatives should the Board consider?

I believe that the communication of critical audit matters would unequivocally be useful to investors and other financial statement users. The purpose of financial statements is to give users pertinent information for decision-making, especially in the case of investors whether or not to invest. Identifying critical audit matters would only serve to assist a user focus on particular issues that would help complete their understanding of the financial statements.

For example, if during the year a company were to make several investments in entities with a less than majority-owned interest, they might have created multiple variable interest entities (VIEs) that would require careful analysis to determine whether the company was the primary beneficiary and thus would need to consolidate them. An auditor might dedicate a significant amount of time testing management's conclusions given the potentially significant balance sheet effects of consolidation, and given the high level of potentially complex judgments involved they might find it necessary to consult with their National office. Ultimately the auditor might obtain reasonable assurance that management's conclusions were accurate. However, given the high degree of judgment and complexity involved on both management and the auditor's parts, an investor might benefit from understanding that such transactions were a significant matter and might be given cause to perform their own due diligence such as performing sensitivity analyses around different scenarios if alternative conclusions could have been made.

11. What benefits or unintended consequences would be associated with the auditor's communication of critical audit matters?; and

13. Could the additional time incurred regarding critical audit matters have an effect on the quality of the audit of the financial statements? What kind of an effect on quality of the audit can it have?

I agree with many of the unintended consequences cited in the Proposed Standard, including the strain on an auditor's work in the final stages of the audit and the potential misunderstanding of critical audit matters by an investing community that is unfamiliar with such disclosure. In the case of strain on an auditor's work, I believe that this risk is minimal given that an auditor's work would likely already contain significant documentation regarding critical matters given existing documentation standards, and in short course this extra step would easily be absorbed into the audit process. I expect the additional time required to address critical audit matters to have, if anything, a positive impact on the quality of the audit by focusing the auditor's

attention on those matters which have a high degree of risk, subjectivity, and/or complexity.

In regards to the potential misunderstanding by the investing community, I believe that the risk of confusing the investing community is greater in the case of not having critical audit matters to guide their focus than in the case of having critical audit matters that an investor inappropriately interprets.

I believe that a far bigger unintended consequence would be the strain critical audit matters could impose on the auditor-client relationship. The auditor-client relationship is already an unusual one in that an auditor is meant to be an external party expressing an opinion on the fairness of a company's financial statements, and yet they are paid by said company, often on-site for extended periods of time, and are able to be fired. I can imagine that management would be incentivized to pressure an auditor into not divulging areas of significant complexity or judgment in a critical audit matter for fear that the investing community would take any such matters as indications of "softer" numbers or aggressive accounting. The auditor would thus be confronted by the pressures to uphold its own professionalism and its desire to maintain a client relationship. In some cases, this might lead to the critical audit matters section being reduced to merely boilerplate language and thus undoing the very spirit of the Proposed Standard to give the investing community additional guidance on how to focus their reading of the financial statements.

15. Would including the audit procedures performed, including resolution of the critical audit matter, in the communication of critical audit matters in the auditor's report be informative and useful? Why or why not?

The audit procedures performed related to a critical audit matter may vary in complexity depending on the matter involved, and in the cases in which audit procedures are exceptionally complex their description may unduly create confusion for the investing community rather than providing illumination on the underlying issue.

On the other hand, in some situations I can imagine that an investor might find the description of certain audit procedures helpful in determining what level of due diligence would be required of their own analysis. For example, if the critical audit matter concerned something like unusual inventory balances, knowing that the auditor performed extensive physical inventory counts might give them less cause to perform sensitivity analyses regarding inventory balances than they would if the auditor performed some form of analytic. Thus, I think the usefulness of disclosing audit procedures will vary case by case but should be guided by the principle that discussion of audit procedures should only occur if it can be done so succinctly *and* if a reasonable investor might draw different conclusions based upon the type of approach used by the auditor.

24. Are there specific circumstances in which the auditor should be required to communicate critical audit matters for each period presented, such as in an initial public offering or in a situation involving the issuance of an auditor's report on a prior period financial statement because the previously issued auditor's report could no longer be relied upon? If so, under what circumstances?

In the spirit of the Proposed Standard, the investing community would be better served if the auditor was required to communicate critical audit matters for each period presented in the situations noted of an IPO or a previous auditor's report no longer being reliable, but *only if* these critical matters were not previously communicated in a public filing. Thus, especially in the case of an IPO where prior periods did not previously communicate critical audit matters, an investor can perform due diligence with full knowledge of where to focus attention in performing analyses for each given year. A company's critical audit matters could very well change from year to year, especially if the company undertook significant acquisitions or changed accounting policies in a given year but not in others. This might give an investor cause to focus their analyses on different aspects of the financial statements for each year in determining their full picture of a company's health.

26. What challenges might be associated with the comparability of audit reports containing critical audit matters? Are these challenges the same for audits of all types of companies? If not, please explain how they might differ.

Critical audit matters will inherently vary from company to company, and it is this very fact that allows an investor to glean company-specific focus. In some industries there will be more variance than others, as some might have a relatively comparable pool of critical audit matters that affect all of them while other industries consist of companies each with unique issues. Regardless, I think this challenge is minimal. Critical audit matters are not meant to radically alter the substance of a company's financial statements, but rather to grant the reader insight into specific areas that might warrant additional attention.

I appreciate the opportunity to share my viewpoint on the Proposed Standard, and I thank you for your consideration of my comments.

Sincerely,

Kevin J. Gomez