AEROSPACE INDUSTRIES ASSOCIATION

December 9, 2013

Office of the Secretary
Public Company Accounting Oversight Board
166 K. Street, NW
Washington DC 20006-2803

Subject: **Proposed Auditing Standards –**

The Auditor's Report on an Audit of Financial Statements when the Auditor Expresses an Unqualified Opinion

The Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report

And Related Amendments to PCAOB Standards

Dear Board:

Thank you for providing the Aerospace Industries Association ("AIA") an opportunity to share our views on your proposed auditing standards – *The Auditor's Report on an Audit of Financial Statements when the Auditor Expresses an Unqualified Opinion, The Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report, and the Related Amendments to PCAOB Standards* (together the "Proposed Standards"), issued by the Public Company Accounting Oversight Board (the "Board") on August 13, 2013. AIA is the premier aerospace industry trade association, representing over 350 of the nation's major manufacturers of commercial, military and business products such as aircraft, helicopters, aircraft engines, missiles, spacecraft, and related components and equipment. Many of the AIA member companies are suppliers to the U.S. Government. AIA previously commented on the *Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards* ("Concept Release") issued by the Board on June 21, 2011.

As previously stated in our September 27, 2011 letter on the Concept Release, we are supportive of the Board's efforts to address the financial reporting concerns of investors and other users of financial statements. However, we continue to believe that improvements to financial reporting can best be achieved through clarifying changes to the audit report by the PCAOB coupled with targeted standard-setting by the Financial Accounting Standards Board ("FASB") or Securities and Exchange Commission ("SEC"). We believe investors and other financial statement users would benefit most from changes to the audit report that clarify the purpose of an audit, the responsibilities of management, and the responsibilities of the auditor. Further, it would be helpful for the audit report to clarify the auditor's existing responsibility with respect to financial information presented outside the financial statements and the applicable PCAOB standards governing their responsibility.

In the following paragraphs, we provide additional feedback on the Proposed Standards.

We believe that the form of the auditor's report should be limited to providing an opinion about whether the financial statements (inclusive of the related notes) present fairly, in all material respects, the financial condition, results of operations, and cash flows of reporting companies in conformity with the applicable financial reporting framework (i.e. pass/fail model).

We believe that the investor concerns cited in the Proposed Standards cannot be adequately addressed in the auditor's report. Rather, these concerns are best addressed by encouraging investors and other users of financial information to read the financial statements in their entirety including Management's Discussion and Analysis ("MD&A") in the 10-Qs and 10-Ks to obtain a complete understanding of the financial health of a company and key risks that could have an adverse impact on financial results. If information contained in the financial statements and MD&A is not useful or is difficult to understand, targeted standard setting should be considered to promote greater transparency and aid in investors' understanding of financial information.

We believe that any Proposed Standards must preserve management's ultimate responsibility for the quality of its financial information and the balance of responsibilities between management and the audit committee for reviewing and certifying the accuracy of that information. Audit committees play a critical role in providing independent review and oversight over a company's financial reporting system and its independent auditors. We firmly believe that management should be the original source of financial information about a company. Both the Management of a company and the audit committee have a very deep knowledge and understanding of its industry, business strategy, and risk factors and their impact on current and future financial results. While an auditor learns a lot about a company's accounting policies and procedures through an audit, their focus is appropriately limited to whether the financial statements are presented in conformity with prescribed accounting rules rather than identifying and classifying the broader business risks (e.g. supply chain, environmental, operational, etc.) that can impact financial results. Any proposal to expand the auditors' role must take care not to dilute or otherwise deemphasize this core responsibility of auditor firms, and it is our view that such a dramatic expansion of the auditor's report risks doing just that.

For many of these same reasons, we oppose the proposed requirement to add a discussion of Critical Audit Matters ("CAM") to the auditor's report. While we acknowledge that the CAM proposal is an improvement over the Auditor's Discussion and Analysis model presented in the Concept Release, we have significant concerns about the operability of the proposal and whether CAM will be useful to investors. Those concerns are as follows:

- We believe drafting of the CAM and documenting why other items weren't included in the CAM could take a significant amount of the auditor's and management's time at a critical point in the process. Furthermore, it could lengthen the timetable between when a company closes its books and files its financial statements with the SEC, increasing audit costs and delaying the release of much anticipated financial information. We believe the additional time and cost required to comply with the proposal would be of little or no benefit to investors.

- We believe discussion of the company's financial information by the auditor could lead to an increase in confusion for the investor by suggesting that the auditor is providing something other than an unqualified audit opinion. We believe that the issuance of an unqualified audit opinion should remain a statement to the investor that all material matters related to the audit have been resolved to the mutual satisfaction of management, the audit committee, and the auditor. We do not believe that discussion about the "most difficult" areas of an audit is relevant if all issues have been resolved to the auditor's satisfaction such that an unqualified opinion is issued. Furthermore, we feel that additional information presented by the auditor may lead to confusion as to which party is responsible for financial information and introduce additional risk for the company and audit firm.

- The definition of CAM is highly subjective and open to interpretation and the inclusion of CAM in an auditor's report may send mixed messages to investors and other users of financial statements. Different accounting firms will likely adopt different practices with respect to matters requiring disclosure as a CAM. Furthermore investors may perceive that an audit report containing no CAM suggests the company being audited has better controls, more transparent disclosures and/or less aggressive accounting positions than a company whose audit report contains multiple CAM. It could also suggest to investors that the accounting firm reporting fewer CAM is not conducting a rigorous audit. We believe that required disclosure of some number of "uncertainties" encountered during an audit – whether or not they are material – could ultimately undermine investors' confidence in financial reporting.

- We have a fundamental issue with a rule that would require the auditor to disclose certain information about a company (e.g. existence of significant deficiencies) that the company isn't required to disclose outside of the audit committee. As previously stated, we believe management should be the original source of all financial information about a company and the auditor's responsibility should be limited to ensuring that financial information is presented fairly and is materially correct.

- We believe that inclusion of CAM in the auditor's report will be, in most cases, duplicative of information already included in the financial statements and MD&A. For example, many companies disclose critical accounting estimates in MD&A based on the enhanced requirements included in a 2002 proposed SEC rule. We believe there is a sufficient amount of detail in those disclosures to let users know that these are highly judgmental areas that are sensitive to changes given certain assumptions. A user of financial statements should be able to infer from the identification of these items that the auditor will spend additional time testing the estimates and discussing assumptions and application of accounting rules with management, the audit committee and potentially the audit quality reviewer. As a result, it is unclear what incremental beneficial information the CAM would provide. Given that the SEC proposal on disclosure about the application of critical accounting policies (SEC Release No. 33-8098) was never issued, investors could benefit from targeted standard setting that would result in the issuance of a final rule applicable to all registrants.

- We believe that linkage of CAM to audit committee communications will potentially impede communications that currently take place between the auditor and the audit committee. We believe that this dialogue is a critical element of the communication process and that without it written words could be taken out of context and used incorrectly in making investment decisions. Furthermore, the knowledge that even discussing an audit matter could result in required audit report disclosure may result in accounting firms becoming more selective about the items they discuss with the audit committee. In Addition, audit committees and/or company officers may be reluctant, to raise concerns or even ask clarifying questions about audit or accounting issues. We believe that the auditor's views should be shared with the audit committee through the existing communication process and that it is ultimately up to management to ensure that disclosures are transparent and fair. Furthermore, we question the impact to the ongoing role of the audit committee if CAM is included in the auditor's report. We believe it could ultimately reduce the dynamic of open dialogue that is critical to effective governance and convert audit committee meetings into formulaic, compliance-driven "check-the-box" sessions.

- As noted above, we believe the CAM identified by the auditor for inclusion in the auditor's report is subjective in nature making it open to unnecessary, but inevitable, challenge by the PCAOB during the inspection process. We are concerned that companies could be required to re-file their financial statements due to a restatement of the audit report, which again will result in additional effort and cost to companies and the auditors, not to mention confusion and uncertainty among investors.

- Requiring disclosure of "challenging" audit matters would also expose companies to increased risk of frivolous lawsuits. Even in cases where generally accepted accounting principles were followed to the letter and any "challenging" issues were resolved to the auditors' satisfaction, the plaintiffs' bar will surely attempt to use any CAM disclosures as de facto admissions of uncertainty or even error in court proceedings. These proceedings, even if they result in no direct liability to the company or its auditors, resulting in increased legal fees to companies, higher audit fees, and investor confusion.

As noted earlier in this letter and in our September 27, 2011 letter on the Concept Release, we would support changes to the audit report that would clarify the auditor's existing responsibility with respect to financial information presented outside the financial statements (e.g., AU sec. 550) and provide reference to PCAOB audit standards or other summary documents that provide additional information about public company audits and auditors (e.g., Center for Audit Quality's published "*In-Depth Guide to Public Company Auditing: The Financial Statement Audit*"). We believe the proposal that the auditor "review and evaluate" other information outside the financial statements and the introduction of new audit procedures is problematic and a step change from what the auditor is responsible for under the current "read and consider" standard, without a demonstrated need for a change.

We are not supportive of these changes for the following reasons:

- We are concerned that the additional costs incurred by the auditor and company to comply with the proposal on other information would far outweigh any benefit received by investors and place an enormous amount of pressure on meeting already tight reporting deadlines. We believe the additional time required for the auditor to perform specific procedures will delay public filings and keep much anticipated financial information from reaching investors and other users of financial statements in a timely manner. It is also unclear as to the operability and cost of the rules as they relate to the proxy, which is typically filed after the 10-K. We are also concerned that this proposal could make the auditor and the company more vulnerable in the event of any future litigation and potentially result in increased audit and legal fees.

- We believe a change from "read and consider" to "read and evaluate" along with the introduction of specific procedures for the auditor to perform would be confusing to investors, perhaps indicating a change in auditor responsibility for other information. Frankly, we believe that this change would be misconstrued to indicate a higher level of assurance is being provided on other information, be it financial or non-financial. We believe that this could result in negative consequences for investors, auditors and registrants.

- We believe the proposals are duplicative of a company's disclosure review policies and procedures. Disclosures are already subject to multiple verification procedures, including CEO/CFO certifications, disclosure committee procedures, formal disclosure controls (subject to

SEC regulation), independent compensation committee certifications, and oversight by independent board committees. We do not understand how auditor review procedures would improve this process and, in fact, are concerned that an overreliance on the auditor could result in a less diligent internal review process.

- We believe the Proposed Standards may have an unexpected impact on the securities law liability rules. In particular, it is not clear whether the proposed "read and evaluate" requirements would expose auditors to additional liability for misstatement and omissions in non-financial disclosures, nor is it clear how new requirements might impact the ability of companies and auditors to rely on the SEC's safe harbor rules applicable to forward-looking information.

- We believe that the extension of auditor responsibility to non-financial information and information incorporated by reference (i.e. proxy) will add additional administrative burden and cost and result in little or no benefit to the investor. We are also concerned that a broadening of auditor focus to information outside their area of expertise or outdated information incorporated by reference could compromise the quality of their audit and reporting on financial information in the financial statements.

- We believe that the proposed expansion of the auditor's scope would be very difficult to implement and confusing for investors and other users. Many areas outside the financial statements are more subjective and less prescriptive than financial statements and as such pose additional challenges for auditors. We question how an auditor will evaluate forward looking information included in MD&A. For example if a company includes earnings guidance in its MD&A will investors be comforted that the auditor has "evaluated" that guidance for material misstatement of fact? Will the auditor be challenged by regulators or users of financial statements if the guidance ultimately proves unreliable? If the auditor has to consent to the reissuance of its report how will it update its commentary on CAM and areas outside of the financial statements?

With respect to auditor tenure, we oppose the proposed requirement to add a statement in the audit report regarding the year the auditor began serving consecutively as a company's auditor. Although the Board indicates that investors and other financial statement users have indicated strong interest in this information, we do not believe the information is relevant or useful in the auditor's report for the following reasons:

- We are not aware of any data indicating a correlation between audit tenure and audit quality, and believe the inclusion of this information in the audit report implies such a correlation exists. Without any context for a user regarding the relevance of this information, each user is left to determine what impact the auditor's tenure has on the conclusions reached by the auditor and expressed in their report. For some, this may simply result in confusion (i.e., they might simply pass over the information since they don't understand why it is being disclosed); however, for others, they may conclude one company's financial statements are more accurate than another's because of differences in audit quality based on one firm's tenure versus another's. In the former case, we don't believe tenure should be included in the report since confusion is certainly not an intended outcome, and in the latter case we don't believe tenure should be in the auditor's report because it could call into question the comparative quality of every audit performed by implying there are higher or lower quality audits performed by firms with different tenures. With mandatory lead and concurring partner rotations as well as the stringent internal quality mechanisms of the firms and external regulation by the PCAOB, we believe the quality of each audit should stand on its own merits regardless of the period of time one firm has been engaged consecutively with a company.

- We recognize that in some circumstances investors may have an interest in understanding the tenure of an audit firm (i.e., at a shareholder's meeting when voting on the engagement of an audit firm). In that circumstance, it would be more relevant in our view to include audit tenure information in a company's proxy statement or some other set of materials that are outside the audit report. Including such information in the audit report shifts a debate over auditor appointment decisions to a debate of the quality of the underlying audit. In our view, provided that an auditor has been engaged according to proper procedures and with adequate oversight, the audit report should be allowed to stand on its own.

With respect to auditor independence, we don't object to inclusion in the auditor's report of a statement stating that the auditor is independent but question the necessity given that the title of the report – "Report of Independent Registered Public Accounting Firm" – indicates that the auditor is independent.

Regarding the other proposed changes; we are supportive of reference to "the related notes" in the introduction paragraph, and clarifying that the financial statements are free of material misstatement, "whether due to error or fraud".

In summary, we are supportive of the Board's efforts to introduce enhancements to the audit reporting model that would meet the needs of investors and be practical for manag*ement, audit committees an*d audit firms to adopt in a cost-effective manner. We believe that the focus should not be on providing more information to investors but rather on providing a higher quality of information to investors. We believe that better information can be provided through a combination of the PCAOB clarifying changes to the audit report coupled with targeted standard-setting by the Financial Accounting Standards Board ("FASB") or Securities and Exchange Commission ("SEC").

We appreciate the opportunity to present our views on this subject and welcome the opportunity to meet in person to review them with you. Thank you for your attention and consideration.

Best regards,

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