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November 14, 2017

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

Re: PCAOB Rulemaking Docket Matter No. 042 – Release No. 2017-005

Dear Office of the Secretary:

RSM US LLP appreciates the opportunity to offer our comments on PCAOB Release No. 2017-005, *Supplemental Request for Comment: Proposed Amendments Relating to the Supervision of Audits Involving Other Auditors and Proposed Auditing Standard, "Dividing Responsibility for the Audit with Another Accounting Firm."* RSM US LLP is a registered public accounting firm serving middle-market issuers, brokers and dealers.

With respect to audits involving other auditors, we continue to support a risk-based supervisory approach focused on significant risks to the consolidated financial statements. The amendments, as proposed to date, have made some strides in that regard, but we believe there are additional opportunities to further promote a principles-based focus on the significant risks, while also allowing the lead auditor to exercise professional judgment in varying the nature, timing and extent of supervisory activities so as to provide for a more effective and efficient audit.

We also support the Board's recent revision that would amend AS 1015, *Due Professional Care in the Performance of Work,* to include a statement that other auditors are responsible for performing their work with due professional care, which concerns what the independent auditor does and how well he or she does it.[1] We believe the overwhelming majority of auditors take the responsibility for due professional care very seriously because they understand that the quality of an audit needed to inspire investor confidence is built on the integrity, competence, objectivity and independence of our profession. We note, however, that certain proposed requirements do not rely on this important premise, but rather, in some instances seem to expect lead auditors to "audit" the other auditor's integrity, competence, objectivity and independence. Although the lead auditor's supervision of the other auditor must involve proper instruction and review, we believe there are areas in which audit quality is best served by the lead auditor relying on the representations made by the other auditor about engagement-specific matters, rather than by requiring the lead auditor to obtain evidence about matters related to the other auditor's system of quality control.

Our comments with respect to the proposed amendments demonstrate how the concept of due professional care can be used effectively in the lead auditor's supervision of the other auditor. Our comments also address other potential enhancements to the risk-based supervisory approach for audits that involve other auditors. Further, we have commented on the effective date of the proposed new auditing standard and amendments.

[1] See paragraph .04 of AS 1015 on page A1-9 of the Release.

Determination to serve as lead auditor (sufficiency of participation)

In the Release, the Board states it is considering revising the provisions for assessing a prospective lead auditor's sufficiency of participation to expressly require consideration of the importance of the locations or business units audited by the lead auditor. We believe the concept of “importance” already is factored into the auditor’s consideration of the risks of material misstatement associated with the portion of the financial statements audited by the lead auditor as required in paragraph .B2.a. of AS 2101, *Audit Planning*. Including importance as an additional consideration would be confusing to apply in practice because “importance” is not defined in the auditing standards; whereas, the consideration of the risks of material misstatement is a familiar concept for auditors and is well supported by the auditing standards. We therefore suggest that paragraph .B2.b. of AS 2101 be deleted.

The Board also is considering adding to paragraph .B2 of AS 2101 another sufficiency threshold to be met by the lead auditor in prospective divided-responsibility engagements as follows:

> In addition, the participation of the engagement partner’s firm to serve as lead auditor ordinarily is not sufficient if the referred-to auditors, in aggregate, audit more than 50 percent of the company’s assets or revenues.

So as to eliminate possible confusion, we believe it would be beneficial if this sufficiency threshold was consistent with the guidance provided for auditors in Section 4140.1 of the SEC Division of Corporation Finance Financial Reporting Manual, and therefore suggest that paragraph .B2 of AS 2101 be revised to read as follows:

> Generally, the lead auditor is expected to have audited or assumed responsibility for reporting on at least 50% of the assets and revenues of the consolidated entity.

Other auditors’ compliance with independence and ethics requirements

We believe the revisions to the proposed requirements in paragraph .B4.a. of AS 2101, which, if finalized, would require the lead auditor to understand each other auditor’s “process for determining compliance” with the SEC independence requirements and PCAOB independence and ethics requirements and experience in applying the requirements, would not be practical to implement for the following reasons:

- Given that the proposed definition of “other auditor”[2] includes both a firm and individuals who are members of the engagement team, proposed paragraph .B4.a of AS 2101 would require the lead auditor to determine each individual’s process for compliance with the independence and ethics requirements. This could entail interviewing all engagement team members and obtaining their requisite records. We do not believe this requirement is practical due to the amount of time involved and the fact that it would be duplicative of what the other auditor firm would already be doing to determine whether individual members of the engagement team are compliant with the requisite independence and ethics requirements. We do not believe such an approach provides a benefit to investors that is commensurate with any potential improvement to audit quality resulting from, or the extensive cost involved with, performing the necessary procedures to comply with the requirement.

[2] See the proposed definition of “other auditor” in paragraph .A5 of AS 2101 on page A2-10 of the Release.

- If proposed paragraph .B4.a. of AS 2101 is interpreted to mean that the lead auditor needs to gain an understanding of the other auditor firm's process for determining compliance (i.e., not the individual's process), we do not think the requirement is practical, given the complexity of, and differences in, each firm's process for determining such compliance. To obtain an understanding of an audit firm's process for determining compliance with independence and ethics requirements would require extensive inquiry of the individual at the firm who is responsible for such matters and also would require reading the firm's policies governing such a process, which, in many instances, could be volumes of material. We do not believe such an approach provides a benefit to investors that is commensurate with any potential improvement to audit quality resulting from, or the extensive cost involved with, performing the necessary procedures to comply with the requirement.
- Paragraph .B4.b(2) is too broadly written and could be interpreted to mean that the other auditor would need to provide the lead auditor with a description of any independence violation related to any client. This would violate client confidentiality requirements and not be relevant to the engagement.

We believe the other auditors' compliance with independence and ethics requirements is best addressed at the engagement level and in reliance upon the due care requirements in AS 1015. We therefore suggest revising paragraph .B4 of AS 2101 to read as follows (proposed deletions are struck through, and proposed additions are shown in bold font):

.B4 In an audit that involves other auditors, the lead auditor should determine each other auditor's compliance with the SEC independence requirements **relative to the audit client** and PCAOB independence and ethics requirements **relative to the audit client** by~~:~~

~~a. Gaining an understanding of each other auditor's (1) process for determining compliance with the SEC independence requirements and PCAOB independence and ethics requirements and (2) experience in applying the requirements; and~~

~~b. Obtaining~~ **obtaining** from each other auditor:

a. ~~(1)~~ A written description of all relationships between the other auditor and the audit client or persons in financial reporting oversight roles at the audit client that may reasonably be thought to bear on independence; and

b. ~~(2)~~ A written representation that it**:**

(1) Has appropriate policies and procedures in place for determining compliance with SEC independence requirements and PCAOB independence and ethics requirements;

(2) Has prepared a self-assessment of compliance with SEC independence requirements relative to the audit client and PCAOB independence and ethics requirements relative to the audit client in accordance with the applicable quality control standards; and

(3) ~~is~~**Is**, or is not, in compliance with SEC independence requirements **relative to the audit client** and PCAOB independence and ethics requirements **relative to the audit client** and, if it is not, a description of the nature of any non-compliance.

Other auditors' knowledge, skill and ability

If finalized, newly proposed paragraph .B6.a. of AS 2101 would require the lead auditor to inquire about other auditors' policies and procedures relating to the (a) assignment of individuals to audits conducted under PCAOB standards; and (b) training of individuals who perform procedures on audits conducted under PCAOB standards regarding the relevant financial reporting framework, PCAOB standards and rules, and SEC rules and regulations. On page 15 of the Release, the Board explains the rationale for this new requirement:

> By understanding the other auditor's policies and procedures for training and assigning its personnel, the lead auditor would be in a better position to identify matters that may warrant further attention. For example, if non-supervisory team members are not required to be trained on PCAOB standards, the lead auditor may decide to obtain additional information about the knowledge, skills, and ability of personnel performing important audit tasks in determining the necessary extent of supervision of their work.

We believe it is the responsibility of supervisory team members to ensure that non-supervisory team members have the requisite knowledge, skill and ability to perform the duties assigned to them. We therefore believe it is unnecessary for the lead auditor to perform the procedures proposed in paragraph .B6.a.of AS 2101 as such procedures would be duplicative of what supervisory team members would do. Further, if the auditor were to perform such procedures and identified matters that warranted further attention, we do not believe it would be practical for the other auditor to "obtain additional information" about such matters for "personnel" because:

- It is difficult for the lead auditor to determine what would be sufficient evidence to demonstrate the knowledge, skill or ability of the individuals. For example, if an individual had a week of training related to PCAOB standards, would that be adequate? Or, should the individual have had two weeks of such training during their career? Would the lead auditor need details about the content of such training?
- Laws in certain jurisdictions, as well as internal firm policies, may prohibit the sharing of confidential employee information outside of the firm.
- We do not believe such an approach provides a benefit to investors that is commensurate with any potential improvement to audit quality resulting from, or the extensive cost involved with, performing the necessary procedures to comply with the requirement.

For these and other reasons, it has been customary for the lead auditor to ask probing general questions about the knowledge, skill and ability of the other auditor, given the scope of the audit, the client's industry and the standards under which the audit is to be performed, among a myriad of other considerations. This dialogue allows the lead auditor to gain an understanding of the knowledge, skill and ability of the other auditors who assist the lead auditor with planning or supervision and who therefore will be responsible for the assignment of individuals to the audit and for ascertaining that those individuals have the requisite training. This manner of asking questions of, and receiving acknowledgments from, the other auditor to determine the other auditor's qualifications is congruent with the notion that other auditors are responsible for performing their work with due professional care.[3]

[3] See the proposed note to paragraph .02 of AS 1015 on page A1-8 of the Release.

We therefore recommend deleting paragraph .B6.a. of AS 2101. If the paragraph is retained, we believe it would be helpful if the amendments would clarify in the definition of “other auditor” the notion that requirements typically would be applied at the firm level, and only would be applied at the individual level for participating persons who are not part of a firm.

Supervising the work of other auditors

Tolerable misstatement

Proposed paragraph .B2.a. of AS 1201, *Supervision of the Audit Engagement*, would require the lead auditor to “Inform the other auditor of…tolerable misstatement.” It appears it is the Board’s intention to require the lead auditor to inform the other auditor of the “tolerable misstatement for the location or business unit.”[4] Therefore, we suggest that paragraph .B2.a. be revised to specify that the required communication is the tolerable misstatement for the location or business unit.

Identified risks of material misstatement

Proposed paragraph .B2.a.(2) of AS 1201 requires the lead auditor to “Inform the other auditor of…the identified risks of material misstatement.” This requirement then becomes the basis for further supervision and review by the lead auditor and for the summary memorandum to be provided by the other auditor. We believe a risk-based approach would not require the communication of all identified risks of material misstatement because not all identified risks of material misstatement will necessarily be applicable to a particular location or business unit and therefore could unintentionally require additional unnecessary procedures by the other auditor. We suggest instead requiring the lead auditor to inform the other auditor of identified *significant* risks of material misstatement *at the entity and business unit level*.

Reviewing the other auditor’s work

Proposed paragraph .B2.b of AS 1201 requires the lead auditor to “Obtain and review the other auditor’s description of the audit procedures to be performed…” We believe this revised new proposed requirement would involve the performance of a review at a level of detail that may not be necessary or effective in all circumstances. For example, it may not be necessary for the lead auditor to obtain the entire audit program from the other auditor when the other auditor performs a full-scope audit for statutory purposes. We believe a more effective and efficient risk-based approach would instead be limited to requiring the lead auditor to obtain and review the other auditor’s description of the nature, timing and extent of audit procedures to be performed in response to identified significant risks of material misstatement at the entity and business unit level.

Likewise, proposed paragraph .B2.d. of AS 1201 would require the lead auditor to “Obtain from the other auditor a summary memorandum describing the other auditor’s procedures, findings, conclusions, and, if applicable, opinion…” We believe a more effective and efficient risk-based approach would instead be limited to requiring the lead auditor to obtain a summary memorandum describing the other auditor’s (a) procedures performed in response to identified significant risks of material misstatement at the entity and business unit level, together with related findings and conclusions; and (b) opinion, if applicable.

Multi-tiered audits

In a multi-tiered audit, proposed paragraph .B3 of AS 1201 requires the lead auditor, in supervising the first other auditor, to “evaluate the first other auditor's supervision of the second other auditor's work.”

[4] See page A4-31 of PCAOB Release No. 2016-002, *Proposed Amendments Relating to the Supervision of Audits Involving Other Auditors and Proposed Auditing Standard—Dividing Responsibility for the Audit with Another Accounting Firm*.

However, the next sentence in that paragraph appears contradictory to the preceding one as it extends the lead auditor's responsibilities beyond evaluating the first other auditor's supervision by requiring the lead auditor to "obtain, review, and retain a copy of the summary memorandum provided by the second other auditor to the first other auditor."

We disagree with the revision to the proposed amendments that would require the lead auditor to obtain, review and retain a copy of the summary memorandum provided by the second other auditor to the first other auditor in a multi-tiered audit. We believe the lead auditor should evaluate the first other auditor's supervision of the second other auditor, but that evaluation should be limited to the lead auditor's review of the information provided by the first other auditor to the lead auditor. In our view, the proposed requirement for the lead auditor to review and retain a copy of the summary memorandum provided by the second other auditor (a) implies that the supervision of the second other auditor by the first other auditor is inadequate; (b) would cause duplicative efforts that would not necessarily improve audit quality; and (c) removes an important exercise of judgment by the first other auditor in discerning which matters are most important to communicate to the lead auditor.

We therefore suggest paragraph .B3 of AS 1201 be revised to read as follows (proposed deletions are struck through, and proposed additions are shown in bold font):

> .B3 In some audits, the engagement team may be organized in a multi-tiered structure. For example, an other auditor might audit the financial information of a location or business unit that includes the financial information of a sub-location or subunit audited by a second other auditor. As another example, an other auditor might assist the lead auditor in supervising a second other auditor. In these situations, the lead auditor may direct the first other auditor to perform the procedures in paragraph .B2 with respect to the second other auditor on behalf of the lead auditor, if appropriate pursuant to the factors in paragraph .06. The lead auditor, in supervising the first other auditor, should evaluate the first other auditor's supervision of the second other auditor's work. **In performing this evaluation, the lead auditor may request information provided by the second other auditor to the first other auditor, as deemed necessary in the lead auditor's judgment.** ~~The lead auditor should obtain, review, and retain a copy of the summary memorandum provided by the second other auditor to the first other auditor (paragraph .B2d). In addition, if the lead auditor directed the first other auditor to perform the procedures in paragraph .B2a, the lead auditor should obtain, review, and retain a copy of the communications required by paragraph .B2a or equivalent documentation of the first other auditor's communication. The lead auditor remains responsible for obtaining, reviewing, and retaining the documentation required by AS 1215.19.~~

Dividing responsibility for the audit with another accounting firm

We agree with the revisions, which now would allow for division of responsibility when financial reporting frameworks are different, as we believe this is an important option that should be allowed to accommodate situations in which a foreign subsidiary's financial statements are prepared in accordance with International Financial Reporting Standards and audited by an other auditor and the consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles.

Communication with audit committees

The Board has proposed revising paragraph 10.e. of AS 1301, *Communication with Audit Committees*, so that the lead auditor is required to communicate to the audit committee the basis for determining the sufficiency of its participation only if significant parts of the audit are performed by other auditors or referred-to auditors. Although this proposed revision is intended to require communication about the sufficiency determination when it is most meaningful, we believe it will lead to diversity in practice because the word “significant” is not defined in the requirement. We therefore suggest the paragraph be revised to read as follows (proposed deletions are struck through):

e. In an audit that involves other auditors or referred-to auditors, the basis for the engagement partner's determination that the participation of his or her firm is sufficient to serve as the lead auditor~~, if significant parts of the audit are to be performed by other auditors or referred-to auditors~~.

Effective date

If finalized, the proposed new auditing standard and amendments will require audit firms a considerable amount of time to develop and implement effective quality control procedures and related training. Also, the new requirements likely will require extensive discussions with other auditors as implementation of the new requirements is evaluated. Due to the extent of these efforts, we believe it would be prudent for the proposed new auditing standard and amendments to be effective for audit periods ending two years after the SEC approves the final standard.

We would be pleased to respond to any questions the Board or its staff may have about our comments. Please direct any questions to Sara Lord, National Director of Audit Services, at 612.376.9572.

Sincerely,

RSM US LLP

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