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Via E-mail: [comments@pcaobus.org](mailto:comments@pcaobus.org)

Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, NW  
Washington, DC 20006-2803

Re: PCAOB Release No. 2016-002, Rulemaking Docket Matter No. 042: *Proposed Amendments Relating to the Supervision of Audits Involving Other Auditors and Proposed Auditing Standard - Dividing Responsibility for the Audit with Another Accounting Firm*

Dear Office of the Secretary:

BDO USA, LLP appreciates the opportunity to respond to the request for comments on the Public Company Accounting Oversight Board's (the PCAOB or the Board) Release No. 2016-002: *Proposed Amendments Relating to the Supervision of Audits Involving Other Auditors* (proposed amendments) and *Proposed Auditing Standard - Dividing Responsibility for the Audit with Another Accounting Firm* (collectively, the Proposal). We support the PCAOB's efforts to strengthen the auditing standards relating to audits in which other auditors participate. As noted in the Proposal, supervision of other auditors presents unique challenges in ensuring an audit is performed in accordance with PCAOB standards, in particular, where other auditors operate in different countries with differing cultures, languages or economic markets, and for this reason, we support enhancing the PCAOB auditing standards to advance audit quality.

As the PCAOB works towards the development of amendments and a new standard relating to the use and supervision of other auditors, we encourage the PCAOB to continue to engage in a dialogue with the International Auditing and Assurance Standards Board (IAASB) to understand the successes and challenges in the implementation of International Auditing Standard (ISA) 600, *Special Considerations - Audits of Group Financial Statements (Including the Work of Component Auditors)*. As noted in the Executive Summary of the Proposal, the IAASB is currently assessing the implementation of ISA 600 and looking to strengthen the standard, and as such, has issued an Invitation to Comment.

In the IAASB's *Invitation to Comment - Enhancing Audit Quality in the Public Interest* (Invitation to Comment), the IAASB notes that regulators and audit oversight bodies have expressed concern about situations where the direction and supervision of the members of the engagement team do not appear adequate and the reviews of their work do not appear to have been performed properly. Similarly, concerns have been raised regarding the direction, supervision and review of the work of other auditors involved in the audit. Based on initial input from responses to the IAASB's Work Plan for 2015-2016 and input from other



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outreach activities, the IAASB is currently exploring whether changes to the requirements and guidance in the ISAs may be necessary in the following areas:

- Strengthening and clarifying how the full suite of ISAs apply in a group audit
- Acceptance and continuance
- Communications between the group engagement team and component auditors
- Using the work of component auditors
- Identifying and assessing risks of material misstatement in a group audit
- Responding to identified risks of material misstatement in a group audit, including issues relating to the group engagement team's involvement in the consolidation process
- Review and evaluation of the work of component auditors

We encourage the PCAOB to monitor the activities of the IAASB relating to this project and align with the IAASB's standards when possible to minimize unnecessary differences.

Our comments below align with the topical sections set out within the Proposal, and as such, our responses to the specific questions posed are addressed, as applicable, within those sections.

### General Comments

Current PCAOB requirements relating to the use and supervision of other auditors in an audit are set forth in AU sec. 543 (reorganized as AS 1205), *Part of Audit Performed by Other Independent Auditors*, and Auditing Standard No. 10 (reorganized as AS 1201), *Supervision of the Audit Engagement*. While AS 1201 was adopted in 2010 as part of the suite of risk assessment standards and addresses the supervision of the audit engagement, AS 1205, last updated in 1972, has not kept pace with the changes in how global companies are structured or operate. Given the growth in the number of companies with global operations, coupled with the increased complexities in the way businesses operate and report financial results, an updated set of standards that reinforces the need for continuing communication and interactions among audit participants, including other auditors, throughout the audit is essential to enhancing audit quality.

While we support enhancing guidance in situations in which other auditors participate in an audit, we believe such enhancements should incorporate a risk-based approach in order to allow the lead auditor to apply professional judgment in developing an audit strategy. We note that the Executive Summary of the Proposal explains that the intention of the proposed amendments are meant to strengthen the PCAOB auditing standards by applying a risk based supervisory approach; however, we believe that the Proposal may be more prescriptive than necessary to achieve its objective. Our comments, in the following section, provide suggestions on how a more-risk based approach to supervision might be accomplished.



## **Proposed Amendments to AS 1201, *Supervision of the Audit Engagement***

### Communication of Risks of Material Misstatement

The proposed Appendix B to AS 1201, *Procedures to Be Performed by the Lead Auditor with Respect to the Supervision of the Other Auditors' Work*, details the procedures the lead auditor is required to perform regardless of assessed risk of material misstatement. We believe such an approach would result in additional work effort without a corresponding benefit. For example, paragraph B2 a. (2) requires the lead auditor to inform the other auditor of identified risks of material misstatement without regard to significance; in essence requiring communication of all risks of material misstatement. We believe such a requirement, without a significance filter and the use of professional judgment, could have a considerable impact and unintended consequence on the extent of work performed by the other auditor beyond what the lead auditor may have intended. To more closely align the proposed requirement with a risk based approach, we suggest modifying the requirement to require communication of *identified significant risks of material misstatement* of the consolidated financial statements, due to fraud or error, *which are relevant* to the work of the component auditor, and the communication of other risks of material misstatement based on the professional judgment of the lead auditor.

### Review of Specified Documentation

The proposed Appendix B to AS 1201, paragraph B2 c. requires the lead auditor to direct the other auditor to provide for review of specified documentation with respect to the work requested, and AS 1215, paragraph 19 lists the documentation related to the work performed by other auditors that the lead auditor must obtain and review and retain, prior to the report release date. AS 1201, paragraph 6 then explains that as part of supervising the audit, the lead auditor would determine the extent of the additional review of the other auditor's work papers necessary. We agree that in certain circumstances, based on an assessment of risk, it would be appropriate for the lead auditor to request to review additional work paper documentation; however, we disagree with the explanation included within the Additional Discussion section of the Proposal (page A4-34). That explanation states, 'For example, the lead auditor could determine it necessary to request additional documentation for review with respect to the work performed by less experienced other auditors, or with respect to an area of heightened risk of material misstatement.' We do not believe the interpretation appropriately considers the extent of supervision and review performed by the engagement partner or senior level team member of the other auditor who oversaw the work performed by the other auditor engagement team members, and believe that the interpretation should be clarified in this regard.

## **Proposed Amendments to AS 1215, *Audit Documentation***

The proposed paragraph .19A of AS 1215 would add a requirement for the lead auditor to include in audit documentation a list of additional work papers of other auditors (beyond those described in paragraph .19) that were reviewed by the lead auditor but not retained that includes a description of the work papers reviewed. We believe the requirement to



include a description of the work papers reviewed is unnecessary, and would result in incremental work effort that does not enhance audit quality. A list that includes the title of the work paper along with a reference to the audit step addressed should provide sufficient context to understand the purpose of the work paper.

**Proposed New Auditing Standard for Dividing Responsibility, AS 1206, *Dividing Responsibility for the Audit with Another Accounting Firm***

We support the development of a separate standard related to dividing responsibility in an audit and the definition of a referred-to auditor. However, we note the Securities and Exchange Commission (SEC) does not use this term and it is unclear how the SEC's term 'principal accountant' aligns with the PCAOB's term, 'referred to auditor,' in situations where responsibility is divided. As such, we believe additional clarity is needed in this regard.

Furthermore, we note that proposed AS 1206 does not permit dividing responsibility in situations where the financial statements of the company's business unit audited by the referred-to auditor were prepared using a different financial reporting framework as the financial reporting framework used to prepare the company's financial statements. We believe this would be a change in practice, as extant standards allow for such reporting, and may have unintended consequences. Current practice allows making reference to another auditor when the measurement, recognition, presentation and disclosure criteria that are applicable to all material items in the subsidiary's financial statements under IFRS are similar to the criteria applicable to all material items in the consolidated financial statements and the lead auditor has obtained sufficient appropriate audit evidence for purposes of evaluating the appropriateness of the adjustments to convert the subsidiary's financial statements to U.S. GAAP. AICPA generally accepted auditing standards (AU-C 600, paragraphs .A54-.A56) provides additional application guidance to assist auditors in determining whether to make reference when the financial reporting framework is not the same, and we believe such guidance would be helpful to practitioners and should also be considered.

**Proposed Amendments to AS 2101, *Audit Planning***

Lead Auditor Determination

The 'lead auditor' is defined in the Proposal as (a) the registered public accounting firm issuing the auditor's report on the company's financial statements and, if applicable, internal control over financial reporting, and (b) the engagement partner and other engagement team members who (i) are partners, principals, shareholders, or employees of the registered public accounting firm issuing the auditor's report and (ii) assist the engagement partner in fulfilling his or her planning or supervisory responsibilities on the audit pursuant to AS 2101 or AS 1201. However, we believe that the definition needs to be broadened to recognize differing firm practices that may allow for personnel sharing between network firms, sometimes referred to as seconded employee arrangements. For example, in some firms, short-term seconded employees, those employed less than six



months, may work on a U.S. public company engagement under the direct supervision of the U.S. engagement partner but retain their employment status with the foreign firm. Under the proposed definition, these seconded employees would be considered part of the other auditor and supervised in accordance with the specified procedures required for these team members due to their designation as 'other auditors.' Such an outcome would not be reflective of the day-to-day supervision of the engagement team, in particular of the seconded employee, and for this reason we believe that seconded employees should be considered part of the lead auditor.

#### Sufficient Participation to Serve as Lead Auditor

Proposed paragraph B2 of AS 2101 explains that in an audit that involves other auditors or referred to auditors, the engagement partner should determine whether the participation of the firm is sufficient to carry out the responsibilities of a lead auditor. In making this determination, the engagement partner is to take into account the risks of material misstatement associated with the portion of the company's financial statements for which the engagement partner's firm performs audit procedures in comparison with the portion audited by other auditors.

While we appreciate the examples provided in Appendix 4 of the Proposal, situations exist such that the circumstances surrounding the determination of sufficiency of the participation of the lead auditor is not always as clear. We note that the IAASB is currently addressing this issue as part of the IAASB's Invitation to Comment. The Invitation to Comment suggested that consideration could be given to clarifying the expected performance requirements for individuals other than engagement partners who sign or who are named in the auditor's report. As an example, they explain that such individuals could at a minimum be expected to perform the same procedures that an EOC reviewer would perform.

We encourage the PCAOB to work with the IAASB in addressing this matter and arriving at a consistent approach.

#### Understanding the Knowledge, Skill and Ability of Other Auditors

The proposed definition of an engagement team includes other accounting firms who perform audit procedures on an audit or assist the engagement partner in fulfilling his or her planning or supervisory responsibilities. As a result, the requirement in AS 1201, paragraph 6 that directs the engagement partner and other team members performing supervisory activities to take into account the knowledge, skill and ability of each engagement team member in determining the extent of supervision, by definition includes supervision of other auditors. We believe that in applying this requirement, the lead auditor should be permitted to apply a risk-based approach as it relates to the other auditor, such that the extent of the lead auditor's procedures to obtain an understanding of the other auditor and the resulting supervision would be less when the lead auditor has determined that the other auditor (1) consistently applies common quality control and monitoring policies and procedures and a common audit methodology, or (2) operates in the same jurisdiction as the lead auditor or



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the lead auditor has prior experience with the other auditor. Applying such an approach would balance the extent of supervision with the assessed risks.

#### Other Comments

##### Other Auditor Responsibilities

We note that the Proposal is focused solely on the requirements of the lead auditor; however, we believe that the two-way communication between the lead auditor and the other auditor could be strengthened, and audit quality improved, through the development of a framework or standard focused on enhancing communication and interaction between the two parties. Additionally we note in practice that there are no formal inter-office reporting requirements and, as a result, the quality of reporting varies. We believe the Board should develop guidance on the content and format of inter-firm reports to promote consistency and help lead auditors understand the work performed and the responsibility taken by the other auditor.

##### Emerging Growth Companies and Applicability of Proposed Requirements to Audits of Brokers and Dealers

We support applying the proposed amendments and new standard to emerging growth companies (EGCs) and brokers and dealers that are required to conduct audits in accordance with PCAOB standards, as we believe the benefits resulting from the Proposal would outweigh any additional costs.

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We appreciate your consideration of our comments and suggestions and would be pleased to discuss them with you at your convenience. Please direct any questions to Chris Smith, National Accounting & Auditing Professional Practice Leader at 310-557-8549 ([chsmith@bdo.com](mailto:chsmith@bdo.com)), Susan Lister, National Director of Auditing at 212-885-8375 ([slister@bdo.com](mailto:slister@bdo.com)), or Patricia Bottomly, National Assurance Partner at 310-557-8538 ([pbottomly@bdo.com](mailto:pbottomly@bdo.com)).

Very truly yours,

/s/ BDO USA, LLP

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