financial executives international

August 30, 2017

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

Subject: PCAOB Rulemaking Docket Matter No. 43

Submitted via comments@pcaobus.org

Dear Board Members,

The Committee on Corporate Reporting ("CCR") of Financial Executives International ("FEI") appreciates the opportunity to comment on the PCAOB's "Proposed Auditing Standard for Auditing Accounting Estimates, Including Fair Value Measurements."

FEI is a leading international organization representing approximately 10,000 members, including Chief Financial Officers, Controllers, Treasurers, Tax Executives and other senior-level financial executives. CCR is a technical committee of FEI, and reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations. CCR member companies represent approximately $7.5 trillion in market capitalization and actively monitor the standard setting activities of the PCAOB.

This letter represents the views of CCR and not necessarily the views of FEI or its members individually.

Executive Summary

CCR is supportive of the efforts being made by the PCAOB to improve the guidance for auditing accounting estimates. However, we ask the Board to consider the implications this proposal would have on the preparer due to increased audit costs, and to specifically reconsider the cost-benefit analysis of the proposed changes.

Pricing Services Concerns

The proposed Appendix 1 provides guidance for auditors using pricing information from pricing services as audit evidence (A4-A8). It is our concern that the guidance, as written, implies auditor's procedures should be based on how particular financial instruments are valued. However, this would be very challenging to operationalize. By and large, companies use reputable pricing services, and when doing so it is not always necessary for management to have insight into how every instrument within the portfolio is valued. If this information is needed by the auditor, the auditor may need to do significantly more work to obtain the information (speak with the pricing service, understand their methodology for each instrument selected for testing, evaluating those methodologies, test the unobservable inputs, etc.) for no perceived benefit. This change could represent a significant shift from what is currently done in practice, and go beyond what we consider necessary. The impact on the preparer is indirect but substantial, as they must provide the auditor with necessary information for their audit evidence/documentation. As this work continues to increase, and consume the time of auditors, it will ultimately also drive increased audit fees.

Practicality of Obtaining Information on Equity Method Investees

Proposed Appendix A to AS1105, *Audit Evidence Regarding Valuation of Investments Based on Investee Financial Condition or Operating Results*, applies to companies with certain investments accounted for by the equity method, investments accounted for by the cost method for which there is a risk of material misstatement regarding impairment, and investments measured at fair value for which the investee's financial condition or operating results are a significant input into the fair value determination. The proposed guidance directs the auditor to consider the financial statements for such underlying investments. The proposed requirements appear to demand a significant increase in the time and demand of final work to be performed by auditors as compared to current practice. Some examples of this include:

Subsequent Events of Investee

Paragraph A3(b) requires the auditor to make inquiries of the *investee* to identify subsequent events and transactions that could be material to the company's financial statement with respect to events and transactions of the investee occurring after the date of the investee's financial statements but before the date of the company's auditor's report.

Current guidance requires auditors to make inquiries of the investor regarding subsequent events. Information relayed by the investor should include all pertinent information—including a subsequent event of an investee that may have a material impact on the investor's financial statements. We question the incremental benefit of the auditor making such inquiries of the investee. Furthermore, in situations where the auditor is unable to obtain the necessary information from the investee, it is unclear whether management will be required to facilitate the conversation between the two parties. This can have broader implications such as higher audit costs and delays in the timing of the audit.

Audit Documentation by Investee Auditor

Proposed paragraph A4(b) requires the auditor to obtain information about the procedures that the investees' auditor performed and the results thereof, or review the audit documentation of the investees' auditor. This applies if the investees' audited financial statements are significant to the valuation of the company's investment. In practice, this would create problems in situations where auditors are required to obtain certain information from an investee but are unable to gather the appropriate information. It is common for an investor to not have a close relationship with an investee, in which case obtaining such information might be difficult. Requiring management to facilitate that dialogue could be extremely challenging and unreasonably burdensome.

Professional Skepticism

It is important that auditors maintain professional skepticism as a key tenant of auditor behavior. Some stakeholders have noted that the language in the proposal may suggest a higher degree of skepticism than is currently required[1], with some suggesting that the auditor is being instructed to be cynical in their approach to management assertions. These concerns are in reaction to the references to "moral hazard" as justifications given for positions taken in the proposal. We recommend clarification that the standards around professional skepticism and due professional care as outlined in existing PCAOB standards continue to apply and that this proposal is not intended to amend, revise, or expand those standards.

Conclusion

Based on the foregoing, we recommend the Board amend the proposal in light of cost considerations these changes will introduce to the preparer, with little perceived benefit to users of financial statements. Requiring more auditing around estimates does not mean better estimates will be provided to users of financial statements. We also ask the Board to consider the tone in which this proposal is written and reinforce the notion of a healthy degree of professional skepticism.

Should you have any questions, we welcome the opportunity to discuss our comments further.

Sincerely,

Mick Homan

Mick Homan
Chairman
Committee on Corporate Reporting
Financial Executives International

[1] Refer to AS 1015: Due Professional Care in the Performance of Work