



KPMG LLP
345 Park Avenue
New York, N.Y. 10154-0102

Telephone +1 212 758 9700
Fax +1 212 758 9819
Internet www.us.kpmg.com

August 30, 2017

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

PCAOB Rulemaking Docket Matter No. 044
Proposed Amendments to Auditing Standards for Auditor's Use of the Work of Specialists

Dear Madam Secretary:

KPMG LLP is pleased to submit comments on the Public Company Accounting Oversight Board's (PCAOB or the Board) Release No. 2017-003, *Proposed Amendments to Auditing Standards for Auditor's Use of the Work of Specialists* (the PCAOB Release or the Proposed Amendments). We welcome the opportunity to work with the Board, PCAOB staff (the Staff), and other stakeholders to improve audit quality through enhanced auditing standards.

Overview

The Board has requested public comment on the PCAOB Release for amending its standards for the auditor's use of the work of specialists. The objective of the Proposed Amendments is to strengthen the requirements for evaluating the work of specialists engaged or employed by a company and to apply a risk-based approach to supervising and evaluating the work of auditor-employed and auditor-engaged specialists.

As noted in the PCAOB Release, the "use of the work of specialists, both by companies and auditors, continues to increase in both frequency and significance."¹ This is in large part due to the increased requirements of financial reporting frameworks to use accounting estimates, including those that are based on fair value measurements. We agree with the Board that audit quality could be improved through enhancement of the PCAOB standards and fully support the Board's efforts to establish a uniform, risk-based approach when auditors use the work of a company's specialist as audit evidence and to

¹ See page 15 of the PCAOB Release

require auditors to apply a risk-based supervisory approach to the use of specialists employed or engaged by the auditor.

The remainder of this letter provides our specific comments on the Proposed Amendments and other matters.

Applicability of Proposed Amendments

We believe that the Proposed Amendments should be applicable to audits of emerging growth companies (EGCs). In our experience, the use of the work of a specialist is common in audits of EGCs. Because users of financial statements of EGCs generally have less visibility into the company, as noted by the Board, and because specialists are often used by auditors when evaluating significant estimates and judgments, there is an increased importance on quality and consistency in the application of auditing standards related to the use of specialists.

Likewise, we also believe that the Proposed Amendments should be applied to audits of brokers and dealers. It is not uncommon for auditors of brokers and dealers to use specialists to address regulatory or valuation matters. We agree with the Board's assertion that having different standards for some entities (i.e., EGCs and brokers and dealers) has the potential to create confusion and may require audit firms to maintain different methodologies for using the work of a specialist.

Definition of a Specialist

For purposes of the Proposed Amendments, a specialist is defined as “a person (or firm) possessing special skill or knowledge in a particular field other than accounting or auditing.”² The Proposed Amendments require assessments of the specialist and the entity that employs the specialist as two separate evaluations. For example, the proposed amendment to AS 1105, *Audit Evidence* (AS 1105), states in paragraph .B3 that “[t]he auditor should obtain an understanding of the professional qualifications of the company's specialist in the particular field, and the entity that employs the specialist (if other than the company).”

We acknowledge that the definition of a specialist is consistent with the current definition in extant AS 1210, *Using the Work of a Specialist*. However, we believe that the definition of a specialist should refer only to an individual and not to a firm. This would be consistent with the different requirements and treatment for assessing a specialist versus the entity that employs the specialist.

² See pages A1-10 and A1-20 of the Proposed Amendments

Use of a Company's Specialist

Assessing the Knowledge, Skill, and Ability of the Specialist and the Specialist's Relationship to the Company

We believe that additional guidance could be included to indicate what the auditor should consider when obtaining an understanding of the professional qualifications of the entity that employs the company-engaged specialist. Paragraph .B3 of the proposed amendment to AS 1105 lists factors to be considered by the auditor when assessing a specialist's knowledge, skill and ability (and such items would help demonstrate compliance with the requirement to obtain an understanding of the professional qualifications of the company's specialist). It is not clear whether these are the same factors that should be considered when obtaining an understanding of the entity that employs the specialist.

In our view, the reputation and expertise of an entity that employs the specialist is an important factor to consider when assessing the specialist's knowledge, skill and ability. We agree with the Board that a strong reputation and standing of the specialist's employer in the specialized field can indicate that the employer maintains qualified staff and that a poor reputation and limited expertise of the employer should result in the auditor increasing its scrutiny when evaluating the qualifications of the individual specialist. We believe reflecting this guidance in the proposed amendment to AS 1105 would assist the auditor when considering the results of the evaluation of the entity that employs the company-engaged specialist for purposes of determining the nature and extent of procedures to be applied when assessing the individual specialist who performs the work that is used by the auditor.

In addition, the proposed amendment to AS 1105 would benefit from guidance on the expected sources of evidence when evaluating a specialist's knowledge, skill, ability, and relationship to the company in accordance with paragraphs .B3 and .B4. Page A3-11 of the PCAOB Release includes potential sources of information that could be incorporated into the relevant amendment. As an example, AS 1105 could address whether the use of a questionnaire provides sufficient evidence by itself with respect to evaluating whether the specialist has a familial relationship with the company. We believe differences in practice could be reduced by including the additional guidance in the proposed amendment to AS 1105.

Evaluating the Work of the Company's Specialist

Paragraph .B8(3) of the proposed amendment to AS 1105 requires the auditor to evaluate whether data was "appropriately used" by the specialist. We believe that additional

clarification is needed as the existing wording may lead auditors to believe they are required to employ or engage a specialist in order to fulfill this requirement. For example, a company's pension specialist uses census data in their models for calculating a company's pension obligation; however, the auditor may not have the expertise to assert that the data was "appropriately used." We suggest that clarifying language be used in the proposed amendment to AS 1105 to state specifically what aspects of the specialist's use of data should be evaluated.

Supervising or Using the Work of an Auditor's Specialist

Assessing the Knowledge, Skill, Ability, and Objectivity of an Auditor-Engaged Specialist

The requirement in paragraph .04 of the proposed amendment to AS 1210, *Using the Work of an Auditor-Engaged Specialist* (AS 1210), to evaluate "whether the specialist or the entity that employs the specialist has ... any other conflicts of interest relevant to the work to be performed" would require the auditor to search for all possible conflicts (due to the use of the word "any"), including those that are not significant or would not impact the judgment of the specialist. In our view, the proposed amendment to AS 1210 should require the auditor to evaluate whether significant conflicts of interest exist based on the procedures performed. If significant conflicts of interest are identified, the auditor should determine whether they could reasonably be expected to influence the judgment of the specialist as it relates to the work to be performed.

In addition, the PCAOB should consider providing guidance within the proposed amendment to AS 1210 about what procedures might be appropriate when assessing whether the specialist and the entity that employs the specialist have the necessary objectivity to exercise impartial judgment on all issues encompassed by the specialist's work related to the audit. Page A3-40 of the PCAOB Release describes sources of information that might be relevant, and we believe it would be helpful to have that guidance included in the proposed amendment to AS 1210.

As previously discussed, we believe a strong reputation and standing of a specialist's employer can indicate that the employer maintains qualified staff and that a poor reputation and limited expertise of the employer should result in the auditor increasing its scrutiny when evaluating the qualifications of the individual specialist. We believe this is equally applicable to specialists engaged by the auditor and that the proposed amendment to AS 1210 would benefit from guidance about the auditor's consideration of the results of the evaluation of the entity that employs the auditor's engaged specialist when determining the nature and extent of procedures to be applied when assessing the individual specialist.

Evaluating the Work of an Auditor-Employed or Auditor-Engaged Specialist

The proposed amendments to AS 1201, *Supervision of the Audit Engagement* (AS 1201), and AS 1210 both make reference to “auditor’s instructions” (see Notes to paragraph .C9 of AS 1201 and paragraph .11 of AS 1210). It would be helpful to clarify whether “auditor’s instructions” is different than establishing an understanding with the specialist of the procedures to be performed (see paragraph .C5 of AS 1201 and paragraph .06 of AS 1210). If these terms are referring to the same concept, then confusion may be avoided if the proposed amendments to AS 1201 and AS 1210 use more consistent terminology. If these are meant to be separate elements, auditors may benefit from an explanation of what the term “auditor’s instructions” encompasses and how that may differ from establishing an understanding of the procedures to be performed, including a statement about the objective and purpose of each requirement.

The examples of situations in which additional procedures are ordinarily necessary to evaluate the work of an auditor-employed specialist (see Note to paragraph .C9 of AS 1201) are the same as the examples for an auditor-engaged specialist (see Note to paragraph .11 of AS 1210). Based on our experience, the report of an auditor-employed specialist would not contain restrictions, disclaimers, or limitations that affect the auditor’s use of the report, and therefore that language could be removed from the Note to paragraph .C9 of AS 1201.

Supervisory Activities

The proposed amendment to AS 1210 uses the phrase “the engagement partner and, as applicable, other engagement team members performing supervisory activities” in various paragraphs. In order to make the linkage more clear, we recommend that a footnote reference to paragraph .04 of AS 1201 be made the first time this phrase is used at paragraph .03 of AS 1210 to clarify that the involvement of “other engagement team members performing supervisory activities” would be subject to the requirements of AS 1201. Adding such reference will assist auditors in their understanding of the responsibilities of the engagement partner and other engagement team members that perform supervisory activities with respect to using the work of an auditor-engaged specialist.

Rescission of Auditing Interpretation 11

Auditing Interpretation 11, *Using the Work of a Specialist: Auditing Interpretation of AS 1210* (AI 11), although not reflective of current accounting requirements and banking regulations, has specific guidance that we recommend be retained and updated.

Alternatively, if AI 11 were to be rescinded, we believe that the proposed amendment to AS 1210 should provide specific guidance on the following matters:

- Considerations of when to obtain periodic updates to legal isolation opinions with the passage of time;
- Considerations of whether a new legal opinion should be obtained for each transaction or whether a prior opinion is sufficient audit evidence;
- The level of affirmation within a legal letter to support the legal isolation criteria (i.e., “would level”);
- Identification of key assumptions embedded in legal opinions regarding legal isolation;
- Examples of adequate and inadequate wording for a legal opinion to support the accounting assertion; and
- An explicit statement that a legal opinion that restricts the use of the opinion to the client, or to third parties other than the auditor, are not acceptable audit evidence.

Rescission of Auditing Interpretation 28

We believe that it would be beneficial if certain portions of Auditing Interpretation 28, *Evidential Matter Relating to Income Tax Accruals: Auditing Interpretations* (AI 28), were retained. The third and fourth question and interpretation of AI 28 provide detailed guidance on who is considered a tax specialist. Because the Proposed Amendments do not include the use of tax specialists within their scope, retention of these portions of AI 28 would help to provide important clarity about the scope of the Proposed Amendments.

Effective Date

We believe that the simultaneous adoption of the Proposed Amendments and the Proposed Auditing Standard – *Auditing Accounting Estimates, Including Fair Value Measurements* and Proposed Amendments to PCAOB Auditing Standards (the Estimates Proposal) would result in significant efficiencies and prevent inconsistencies in their application. The use of a specialist in an audit frequently occurs in connection with auditing an accounting estimate, and the Proposed Amendments and the Estimates Proposal include references to each other.

If final amendments are approved by the SEC on or before June 30, 2018, we would support the amendments becoming effective for audits of periods ending on or after December 15, 2019. We believe this would allow sufficient time for audit firms to make the necessary adjustments to their system of quality controls and update their methodologies, guidance, tools, and templates and to develop and provide training.

Editorial Comments

We provide the following editorial comments to the Staff for its consideration (deletions, where applicable, are struck through in bold and additions are underlined).

Paragraph .B8 of AS 1105 – “... external sources and used by the specialists, and ...”

Proposed amendment to AS 1201 – A specialist employed by the auditor is defined in paragraph .C1 of AS 1201 as an auditor-employed specialist, yet that defined term is not subsequently used in paragraphs .C5 and .C7-.C9 (instead the general term of “specialist” is used). We recommend that the defined term of “auditor-employed specialist” be used, where applicable, in those paragraphs.

Paragraph .C8 of AS 1201 – “...provides sufficient appropriate audit evidence. Specifically, the engagement partner and, as applicable, other engagement team members performing supervisory activities should evaluate whether: ...”

Proposed amendment to AS 1210 – A specialist engaged by the auditor’s firm is defined in paragraph .01 of AS 1210 as an auditor-engaged specialist, yet that defined term is not subsequently used in paragraphs .03-.11 (instead the general term of “specialist” is used). In addition, paragraph .08 of AS 1210 introduces a new term (“auditor’s specialist”). We recommend that the defined term of “auditor-engaged specialist” be used, where applicable, in those paragraphs.

We appreciate the Board’s and Staff’s careful consideration of our comments, and welcome the opportunity to discuss our comments further with the Board and Staff. If you have any questions regarding our comments included in this letter, please do not hesitate to contact Rob Chevalier (212-909-5067 or rchevalier@kpmg.com).

Very truly yours,

KPMG LLP

Office of the Secretary
Public Company Accounting Oversight Board
August 30, 2017
Page 8

cc:

PCAOB

James R. Doty, Chairman
Lewis H. Ferguson, Board Member
Jeanette M. Franzel, Board Member
Steven B. Harris, Board Member
Martin F. Baumann, Chief Auditor and Director of Professional Standards

SEC

Jay Clayton, Chair
Michael S. Piwowar, Commissioner
Kara M. Stein, Commissioner
Wesley Bricker, Chief Accountant
Julie A. Erhardt, Deputy Chief Accountant
Marc A. Panucci, Deputy Chief Accountant
Sagar S. Teotia, Deputy Chief Accountant