Dear Public Company Accounting Oversight Board,

I find that the proposal of Public Company Accounting Oversight Board to implement two new reporting standards in order to align the information held by the auditor with the information needed by an investor is a great initiative to make the auditor’s statement not only indicative of the pass/fail status of a company’s annual statement, but also more communicative.

The newly proposed standards imply that the auditor identifies critical issues, which he/she have been working at with a management of a company. In case when the auditor finds inconsistency or material misstatement of fact, the auditor is proposed to request management to revise the other information to address the issues. to make informed decision on a company’s financial standing.

First, I particularly support the standard of highlighting the issues of auditor’s main concern while working with a company’s management. My five-year experience in financial statement analysis has taught me that sometimes the most important information is not contained in financial statements, which financial analysts use to conduct valuations and make investment decisions. While an auditor develops a close relationship with a company and a deep understanding of its operation processes, a financial analyst does not have such an advantage. Therefore, including highlights of the possible problematic issues of a company in the auditor’s report will help an analyst to draw upon the profound expertise of an auditor and his/her knowledge of a specific company.

Second, many important issues of a company’s operations and financial performance are hard to find in the statements themselves. They are often included in the notes to financial statements. Sometimes they do not even have a clear uniform structure for all public companies, which makes benchmarking and financial analysis difficult.

Third, there are several issues which could be used for manipulation of a company’s results, and which are not included in financial statements at all. For example, transactions between a company and its franchisees could be recorded in several different ways, which will ultimately affect costs and net income from operations. While an auditor, who works with the management obtains information on the nature of the company’s relationships with its franchisees, an analyst does not. The other example is an acquisition of a subsidiary and consolidated financial reporting. A financial analyst often does not have information on the nature of the acquired business, while the auditor has a chance to request it. The nature of contracts and the timing of payments is also not explained in the reports and could be used to manipulate the results.
Having mentioned these advantages of the new reporting standards proposed by the Public Company Accounting Oversight Board, I would like to also mention a concern with the incentives provided under the new reporting standard.

I believe that the proposed informative disclosure might lead to a disincentive for management to cooperate with an auditor in cases when the reporting is fair and transparent. In other words, cooperative management will be penalized under the proposed auditor reporting format. Under the new standard, the auditor lists all the areas, in which he/she cooperated with the management of a public company to make audit reporting more transparent. If the cooperation between the two parties was extensive, the shareholders will see a long list of issues, which might alarm them. Thus, management can be penalized by the shareholders’ discontent for cooperating with an auditor and providing documents for more transparency.

In conclusion, I hope that the new initiative will quickly gain momentum, so that auditors’ expertise could be drawn upon by the investor community.

Best Regards,
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