PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

(PCAOB)

STANDING ADVISORY GROUP MEETING

9:03 a.m.

Wednesday, October 14, 2009

National Association of Home Builders

1201 15th Street, N.W.

Washington, D.C.
input. And Damon, thanks also for the commentary on fraud.

Let's move along to the second topic where we have issued a concept release on confirmations, and Dee Mirando-Gould is going to give you a summary of the comments received there.

Thanks, Dee.

DEE MIRANDO-GOULD: Thank you, Marty.

So, as you are aware, we spoke with the SAG last April regarding confirmations, and we released a concept release in the middle of April. The comment period ended May 29th, and we received 24 comments. The majority of those comments again are from firms or associations of accountants, and then there is a smattering of academics, issuers, other standard setters, other organizations, and the like in those comments.

And similar to Keith's comments, I just want to go through some discussion of some key themes with those comments. Generally, commenters were supportive of the PCAOB considering revising its standard on confirmations, and that was mostly because of changes in technology that didn't exist at the time the original standard was put in place.

A number of commenters, a lot of auditors referred us to the IAASB standard ISA 505, which deals with confirmations, and the ASB's proposed statement on auditing standards, which came out at the end of May of this year, to look to try to align with those standards and also be more principles based in our approach. So not include a lot of additional requirements in the standard is what was recommended to us.

We were also recommended to focus on risk, make the standard be based on -- the use of confirmations be based on an auditor's risk assessment. And then, as a general comment, we received a lot of support for revising the definition of confirmation. In the concept release, we asked the question whether or not confirmation should be revised and should include direct access to information held by a third party on behalf of a confirming party? And overwhelmingly, the commenters supported us revising the definition incorporating direct access as a confirmation.
Meeting on the area of confirmations, any concerns that people think we need to consider.

PAUL BESWICK: And this will be very brief. It seems to me the divergent views on expanding the presumption beyond accounts receivable would be contrary to the previous slide, where you say it should be risk based. If it's risk based, they will determine when they need to do something beyond accounts receivable.

So I can't quite understand why the academics would be arguing to do more because of risk if it's already covered on the previous slide?

DEE MIRANDO-GOULD: If I can just answer that? I think the issue there was that there are certain areas, like investments and certain revenue transactions and the like, that individual commenters thought were riskier areas in the first place so that the auditor should confirm those types of things because they are higher risk, and that would go along the lines of the risk focus.

But I take your point. I understand the confusion there.

standard should include something around that standard should include something around that.

Any other comments, thoughts?

ELIZABETH GANTNIER: It seems that all the themes I'm hearing today are auditors don't understand how to evaluate the risk of fraud. Auditors don't know how to evaluate when the risk is great enough that a third-party independent confirmation is required. Auditors don't understand, and we'll get later to how to evaluate fair value properly or related party transactions properly.

And I guess I'm waiting for a conversation about how we're going to train auditors in these processes, and yet all I'm hearing is so let's just default to a standard that requires or presumes certain risk assessments, which goes against pretty much everything that I know about auditing is that you're supposed to be capable of evaluating risk and employing your time and resource properly to these items.

And I wish there was a place in all of this where we said we don't have to answer every failure by an auditor with a standard that requires a presumption that something is, therefore, high risk. We had to...
redo Audit Standard 2 because it was so prescriptive, and it had so much "If you have this, then it is a material weakness." And we backed off of that and said, for example, these are examples of what might be a material weakness. But we got rid of the "always" and "never" type of language.

And so, again, I just wish there was a place in all this where students were better trained in risk assessment and audit technique and theory and less about presumption in the standards about you have to confirm something. That ought to be left to us to decide.

Keith Wilson: Can I just react to that a little bit? At least from the standpoint of risk assessment, I take your point about a large number of presumptions. Certainly I think one of the things that we tried to do with the risk assessment standards is to lay out these points for discussion and say have these risen to the point where they’re important enough often enough that there ought to be a presumption here? It’s a point of discussion. It doesn’t necessarily mean that that’s the intention, okay? So

Martin Baumann: And the last comment, I’d like to make is that --

Dee Miranda-Gould: Sam?

Martin Baumann: -- of course, Dee was putting up some of the responses we got back and not necessarily how we’re going to deal with those responses. But there were some mixed views with respect to the presumptions. She was just commenting forth a process that allows the auditor to demonstrate that they have a reasonable basis for those risk assessments, okay, and then they can develop -- and how they can develop responses that are commensurate with the risk.

So I think that is an approach that we’re trying to follow. But for purposes of standard-setting and discussion, I think sometimes it’s helpful to just lay out these points for discussion and say have these risen to the point where they’re important enough often enough that there ought to be a presumption here? It’s a point of discussion. It doesn’t necessarily mean that that’s the intention, okay? So

Martin Baumann: And the last comment, I’d like to make is that --

Dee Miranda-Gould: Sam?

Martin Baumann: -- of course, Dee was putting up some of the responses we got back and not necessarily how we’re going to deal with those responses. But there were some mixed views with respect to the presumptions. She was just commenting forth a process that allows the auditor to demonstrate that they have a reasonable basis for those risk assessments, okay, and then they can develop -- and how they can develop responses that are commensurate with the risk.

So I think that is an approach that we’re trying to follow. But for purposes of standard-setting and discussion, I think sometimes it’s helpful to just lay out these points for discussion and say have these risen to the point where they’re important enough often enough that there ought to be a presumption here? It’s a point of discussion. It doesn’t necessarily mean that that’s the intention, okay? So

Martin Baumann: And the last comment, I’d like to make is that --

Dee Miranda-Gould: Sam?

Martin Baumann: -- of course, Dee was putting up some of the responses we got back and not necessarily how we’re going to deal with those responses. But there were some mixed views with respect to the presumptions. She was just commenting forth a process that allows the auditor to demonstrate that they have a reasonable basis for those risk assessments, okay, and then they can develop -- and how they can develop responses that are commensurate with the risk.

So I think that is an approach that we’re trying to follow. But for purposes of standard-setting and discussion, I think sometimes it’s helpful to just lay out these points for discussion and say have these risen to the point where they’re important enough often enough that there ought to be a presumption here? It’s a point of discussion. It doesn’t necessarily mean that that’s the intention, okay? So

Martin Baumann: And the last comment, I’d like to make is that --

Dee Miranda-Gould: Sam?

Martin Baumann: -- of course, Dee was putting up some of the responses we got back and not necessarily how we’re going to deal with those responses. But there were some mixed views with respect to the presumptions. She was just commenting forth a process that allows the auditor to demonstrate that they have a reasonable basis for those risk assessments, okay, and then they can develop -- and how they can develop responses that are commensurate with the risk.

So I think that is an approach that we’re trying to follow. But for purposes of standard-setting and discussion, I think sometimes it’s helpful to just lay out these points for discussion and say have these risen to the point where they’re important enough often enough that there ought to be a presumption here? It’s a point of discussion. It doesn’t necessarily mean that that’s the intention, okay? So

Martin Baumann: And the last comment, I’d like to make is that --

Dee Miranda-Gould: Sam?

Martin Baumann: -- of course, Dee was putting up some of the responses we got back and not necessarily how we’re going to deal with those responses. But there were some mixed views with respect to the presumptions. She was just commenting forth a process that allows the auditor to demonstrate that they have a reasonable basis for those risk assessments, okay, and then they can develop -- and how they can develop responses that are commensurate with the risk.

So I think that is an approach that we’re trying to follow. But for purposes of standard-setting and discussion, I think sometimes it’s helpful to just lay out these points for discussion and say have these risen to the point where they’re important enough often enough that there ought to be a presumption here? It’s a point of discussion. It doesn’t necessarily mean that that’s the intention, okay? So

Martin Baumann: And the last comment, I’d like to make is that --

Dee Miranda-Gould: Sam?

Martin Baumann: -- of course, Dee was putting up some of the responses we got back and not necessarily how we’re going to deal with those responses. But there were some mixed views with respect to the presumptions. She was just commenting forth a process that allows the auditor to demonstrate that they have a reasonable basis for those risk assessments, okay, and then they can develop -- and how they can develop responses that are commensurate with the risk.

So I think that is an approach that we’re trying to follow. But for purposes of standard-setting and discussion, I think sometimes it’s helpful to just lay out these points for discussion and say have these risen to the point where they’re important enough often enough that there ought to be a presumption here? It’s a point of discussion. It doesn’t necessarily mean that that’s the intention, okay? So
should not take without a great deal of soul searching.

MARTIN BAUMANN: Good. Thanks for that input, Sam.

Randy Fletchall?

RANDY FLETCHALL: Gosh, after that, I hate to go back to confirmations, Sam.

[Laughter.]

RANDY FLETCHALL: But you mention there about disclaimers and restrictive language, and we've talked about that stuff at the last meeting in terms of seeing more of that and how to evaluate whether that was to such extent that you really couldn't treat it as audit evidence.

I guess the other thing is also we've seen increasing is where companies just won't respond. And whether that's kind of a misinterpretation of Section 303 of Sarbanes-Oxley or not, I guess I would make sure, as you write your standard, not only deal with disclaimers and restrictions, but where you just recognize you're using confirmations more often and yet maybe respondents are not required to send them back to you.

And I don't have a solution here because, you know, public companies, nonpublic, individuals -- it's not like there's any one group that can dictate that people have to respond. But I would encourage you in the standard itself or covering releases to recognize that as you talk about it is good evidence, try to use it more often, that you're going to have to deal with situations where you are unable to get a response and have to do alternative work to satisfy the evidential matters.

DEE MIRANDO-GOU LD: Thank you, Randy.

As you may be aware, in the comments we've received, we certainly received a lot of suggestions that we consider response rates and we consider disclaimers and consider whether or not there's anything we can do, as a group, to help improve that. So it's certainly something that we haven't forgotten and we are considering in the whole process as we go down this path.

Yes. We appreciate it.

MARTIN BAUMANN: Thanks for your comments on that.
Meeting of the Standing Advisory Group

October 14, 2009
9:00 a.m. – 2:30 p.m.
Update on Proposed Standards and Concept Release Issued

Keith Wilson, Dee Mirando-Gould, and Bella Rivshin

Associate Chief Auditors, Office of the Chief Auditor
Update on Proposed Standards and Concept Releases

- Proposed standards on risk assessment
- Audit confirmations concept release
- Signing the auditor’s report concept release
Audit Confirmations Concept Release

Comment Letters Received

- Firms and association of accountants 15
- Academics and associations of academics 1
- Issuers, business groups, and internal auditors 1
- Investor representatives 1
- Other standards-setters 1
- Other organizations 2
- Other individuals 3

Total 24
Key Themes of Comment Letters

- Support for a revised standard
- Standard should be principles-based
- Confirmation should be a function of risk assessment
- Support alignment with ISA 505 and the ASB’s Proposed Statement on Auditing Standards
- Support for revising definition of confirmation to include direct online access and exclude oral responses
Audit Confirmations Concept Release

Key Themes of Comment Letters (cont’d)

- Requirement to request confirmation
  - Divergent views on expanding the presumption beyond accounts receivable
- Disclaimers and restrictive language
  - Clarify auditor’s responsibility to evaluate
  - Provide more guidance on how language affects audit evidence
- Negative confirmations should be permitted as audit evidence