

January 20, 2004  
Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, N.W.  
Washington, D.C. 20006-2803

**Re: PCAOB Rulemaking Docket Matter No. 012, *Proposed Auditing Standard On Audit Documentation And Proposed Amendment To Interim Auditing Standards***

Dear Mr. Secretary:

The American Institute of Certified Public Accountants (“AICPA”) respectfully submits the following written comments on the Public Company Accounting Oversight Board’s (“PCAOB” or “Board”) proposed auditing standard on documentation entitled *Audit Documentation* (the proposed standard). Our comments reflect our views as they pertain to audits of issuers subject to the Act and do not necessarily reflect our viewpoint for audits of nonissuers. The AICPA is the largest professional association of Certified Public Accountants in the United States, with more than 330,000 members in public practice, business, industry, government, and education.

### **Executive Summary**

The AICPA recognizes the effort put forth by the PCAOB to implement the provisions of the Act and enhance professional standards. The PCAOB’s efforts are an important element in restoring public confidence in audited financial statements of public companies. The establishment and maintenance of high quality auditing and other professional standards is critical to that goal. The AICPA is committed to working cooperatively with the PCAOB in the continuous improvement of auditing standards.

We believe that incorporating our recommendations into the final standard will improve implementation of the requirements of the Act both by auditors and issuers. Our more significant concerns with the proposed standard are the following:

### **Auditor Judgment**

The PCAOB’s release states that the proposed standard would adopt the essence of U.S. Government Accounting Office’s (GAO) documentation standard for government and other audits conducted according to generally accepted government auditing standards. However, the GAO documentation standard acknowledges the role of professional judgment regarding the

quantity, type, and content of audit documentation—the PCAOB’s proposed standard does not.

While eliminating the auditor’s ability to exercise professional judgment regarding documentation matters will indeed facilitate enforcement actions, we question whether, and if so how, such elimination will improve audit effectiveness on *all* audits. Our detailed comment on this issue appears in the attachment to this letter (see comment on paragraph 1).

### **Experienced Auditor**

The proposed standard requires auditors to prepare documentation that will enable an “experienced auditor” to understand the work and conclusions reached in an audit engagement. An engagement partner’s years of on-the-job experience and training are among the competencies that give him or her the ability to exercise the critical judgments and to reach the conclusions that are required in an audit engagement, especially in complex or very large engagements. Any other auditor who doesn’t possess a level of experience and knowledge of the client’s industry and business that is equivalent to that of the engagement partner lacks the capacity to evaluate the judgments and conclusions reached by the engagement partner and should not be considered an experienced auditor. Our detailed comment on this issue appears in the attachment to this letter (see comment on paragraph 5).

### **Implementation Date**

The standard applies to all engagements completed on or after June 15, 2004. Many of the engagements that auditors will complete on or shortly after June 15 may already be underway. That means that auditors on those engagements should be documenting their work in accordance with a standard that is in its exposure phase and has not yet been approved by the PCAOB or the SEC. We question whether this is consistent with the PCAOB’s standards-setting process. Our detailed comment relating to this issue appears in the attachment to this letter (see comment on paragraph 18).

Details of our recommendations relating to the above as well as other recommendations are attached to this letter.

We appreciate the opportunity to comment on the proposed statement, and would be pleased to meet with Board members and staff to discuss our comments.

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Sincerely,

A handwritten signature in black ink, appearing to read "S. Scott Voynich". The signature is written in a cursive style with a prominent initial "S".

S. Scott Voynich, CPA  
Chairman of the Board

A handwritten signature in black ink, appearing to read "Barry C. Melancon". The signature is written in a cursive style with a prominent initial "B".

Barry C. Melancon, CPA  
President and CEO

# ATTACHMENT

## Specific Comments

### PCAOB Proposed Auditing Standard, *Audit Documentation*

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#### Paragraph 1

According to the PCAOB's release, the proposed standard adopts the substance of the documentation standard in the United States General Accounting Office's *Government Auditing Standards* (also known as the Yellow Book). That standard acknowledges the role of auditor judgment in the determination of the quantity, type, and content of audit documentation. Specifically, paragraph 4.23 of the Yellow Book states that "The form and content of audit documentation should be designed to meet the circumstances of the particular audit....The quantity, type, and content of audit documentation are a matter of the auditors' professional judgment."

In view of the fact that the PCAOB derived the substance of the proposed standard from the GAO's documentation standard, we found it surprising then that the PCAOB proposed standard does not acknowledge the role of the auditor's professional judgment in the determination of the quantity, type, and content of audit documentation. The application of professional judgment is necessary in identifying the procedures, evidence, and conclusions that are relevant to the audit and therefore should be documented. It is impractical or impossible to document every aspect of a complex audit engagement.

*Accordingly, we recommend adding language to the proposed auditing standard similar to the cited language from the Yellow Book. Also, to aid auditors in making the necessary judgments regarding documentation, the final standard should include language similar to the language in paragraph 7 of the interim standard on audit documentation that states:*

In determining the nature and extent of the documentation for a particular audit area or auditing procedure, the auditor should consider the following factors:

- Risk of material misstatement associated with the assertion, or account or class of transactions
- Extent of judgment involved in performing the work and evaluating the results
- Nature of the auditing procedure
- Significance of the evidence obtained to the assertion being tested
- Nature and extent of exceptions identified
- The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed

*This guidance would supplement the guidance in paragraph 5 of the proposed standard.*

## **Paragraph 2**

This paragraph states that audit documentation “provides the basis for the review of the quality of the work by providing the *reviewer* [emphasis added] with written documentation of the evidence supporting the auditor’s significant conclusions.”

*We recommend specifically identifying the reviewer as any one of the individuals identified in paragraph 3a-c of the proposed standard. (See also our comment on paragraph 3.)*

## **Paragraph 3**

Item *f* of paragraph 3 implies without any basis that the auditor has an obligation to provide to other unspecified individuals information that is useful to their purpose or grant access to all audit documentation. It further improperly suggests that these unspecified third parties are entitled to review all audit documentation. Auditors do not consider the needs, and it is impractical and likely impossible to do so, of these unspecified third parties when preparing documentation during the audit because their needs are unknown at the time the documentation is prepared. Additionally, audit documentation contains a significant amount of confidential client information and information on audit processes proprietary to the accounting firm. Auditors are often required by state law or regulation, and professional Codes of Conduct to maintain the confidentiality of that information and for that reason need to limit the access of others who are not subject to the same standard of confidentiality as the auditor.

We therefore recommend deleting item *f* of paragraph 3.

## **Paragraph 4**

This paragraph contains examples of audit documentation. With one notable exception, the list of items is similar to the one in the interim auditing standard on documentation. The notable exception is *audit programs*. Audit programs generally provide the principal record of the audit procedures the auditor plans to perform, and the auditor initials and dates them to indicate who performed the work. Therefore, the audit program meets the objectives of audit documentation described in paragraph 2 of the PCAOB’s proposed documentation standard.

*We recommend adding audit programs to the examples of audit documentation in paragraph 4. If the PCAOB’s position is that audit programs are not audit documentation, or should not be used for certain purposes, it should specifically state so in the final standard.*

**Paragraph 5** This paragraph requires documentation to contain sufficient information to enable an “experienced auditor, having no previous connection with the engagement: to understand the nature, timing, extent, and results of the procedures performed, evidence obtained, and conclusions reached....”

Audit engagement partners are often individuals with significant years of experience in the client's industry and often have a substantial amount of accumulated knowledge of the client's operations or those of a comparable entity, as well as of the business and financial statement risks affecting the client or similar entities in the client's industry. This experience enables engagement partners to make the necessary judgments and decisions in an audit. An individual whose audit experience isn't at least equivalent to the experience level required of a partner or concurring reviewer (e.g., industry, client operations), lacks the capacity to evaluate that partner's judgments and conclusions.

*We recommend specifically indicating that the "experienced auditor" contemplated by the standard is an individual whose competencies would have otherwise enabled him or her to serve as engagement or concurring partner on the engagement.*

### **Paragraph 6**

**Specialists:** It is unclear whether the "specialists" referred to in this paragraph are audit firm employees with special skills, outside specialists hired by the auditor for certain aspects of the audit, or both. Outside specialists may not be CPAs and therefore may be unfamiliar with, and not required to abide by, the documentation standards governing financial statement audits, including those of the PCAOB. Also, the auditor may be unable to obtain the outside specialist's documentation.

*Because the proposed standard's jurisdiction is over auditors/audit firms registered with the PCAOB and outside specialists are not required to register with the PCAOB, we recommend deleting from paragraph 6 the phrase "including any specialists". If the PCAOB wishes to require specific documentation relating to the work of a specialist who is not an employee of the firm, it should consider adding detailed documentation requirements to SAS No. 73, Using the Work of Specialists.*

**Rebuttable presumption:** The proposed standard states that the presumption that if audit work was not documented it was not performed is rebuttable by *persuasive other evidence* that the procedures were applied and the evidence was obtained.

*We recommend clarifying or providing examples in the final standard of what the PCAOB considers persuasive other evidence. This is especially important in view of the statement in the PCAOB's release that "...oral explanation alone would not constitute persuasive other evidence..."*

### **Paragraph 9**

The definition of *audit adjustment* in the proposed standard is inconsistent with the definition of audit adjustment that is currently elsewhere in the PCAOB's interim auditing standards (see paragraph 9 of SAS No. 61, *Communication With*

*Audit Committees.* Additionally, the definition in the proposed standard is expressed in terms of a financial statement misstatement's effect on the company's "financial reporting process." This reference to financial reporting process seems more appropriate in the context of item *b* of paragraph 9.

*We recommend deleting everything but the first sentence in item c of paragraph 9. If the PCAOB retains all of the guidance in this item, we suggest that it clarify what it means by "material effect on the company's financial reporting process [emphasis added]" since this item seems to already be addressed in item b of paragraph 9.*

### **Recommended addition to the guidance in paragraph 13**

As indicated in our comment on paragraph 3, auditors are bound by state law and regulation, and professional Codes of Conduct that require them to maintain confidentiality of client information. Audit documentation contains a significant amount of confidential client information. In addition, most states recognize the auditor's right of ownership of the documentation and this also helps to maintain confidentiality. Individuals outside of the audit firm are not bound by the same confidentiality provisions as auditors.

*We recommend specifically stating in the final standard that audit documentation is the property of the auditor in order to enable the auditor to fulfill his or her professional responsibilities regarding confidentiality of client information and to ensure the proper continuous custody of the documentation. Additionally, we suggest language similar to the language in paragraphs 11 and 12 of the interim audit documentation standard to specifically recognize the auditor's confidentiality obligation. Those paragraphs state as follows:*

11. The auditor has an ethical, and in some situations a legal, obligation to maintain the confidentiality of client information...Because audit documentation often contains confidential client information, the auditor should adopt reasonable procedures to maintain the confidentiality of that information.
12. The auditor also should adopt reasonable procedures to prevent unauthorized access to the audit documentation.

### **Paragraph 14**

The 45 day deadline for assembling audit documentation is burdensome, especially for certain types of engagements and at certain times of the year (e.g., "busy season"), especially in light of the current implementation date for the Section 404 requirements and the requirement to include sufficient documentation of the work performed by other auditors, which may include foreign affiliates.

*We recommend extending this period initially to at least 60 days until procedures and best practices can be put in place to facilitate the 45 day deadline.*

### **Paragraph 17**

As written, the paragraph could be interpreted to classify as *audit documentation* documents and information that are not considered audit documentation by the Securities and Exchange Commission (SEC) requirement cited in footnote 4 to paragraph 17.

*We recommend changing the example cited in footnote 4 or more specifically limiting the example to the records in the SEC requirement that constitute audit documentation for purposes of the proposed standard.*

### **Paragraph 18**

If the proposed effective date is implemented as proposed, the requirements of the proposed standard would be considered to be in effect since the beginning of the exposure period although it has not yet been approved as a final standard by the PCAOB or the SEC. That is because the audits to which the standard applies are currently underway. We believe it impractical to retroactively apply a standard such as this one on documentation, as it may not be possible to retroactively obtain certain temporal information or documents or create a transcript of past discussions, conversations or meetings. We believe this aspect of the proposal is inappropriate and question whether it is consistent with the PCAOB's standards-setting process.

*We recommend changing the effective date of the final standard to allow the audit firms adequate time to develop procedures and staff training to effect an orderly implementation of the standard. The new standards should be effective for periods beginning no sooner than 60 days after the publication of the final standard.*

### **Minor Editorial Observations**

Paragraph 7a: Should "audit" be "auditor"? And if so, how does the auditor demonstrate "how" he or she complied with all auditing and related professional practice standards?