

February 18, 2009

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

By e-mail: [comments@pcaobus.org](mailto:comments@pcaobus.org)

**Re: PCAOB Release No. 2008-006 – Proposed Auditing Standards Related to the Auditor’s Assessment of and Response to Risk (PCAOB Rulemaking Docket Matter No. 026)**

Dear Mr. Seymour:

The New York State Society of Certified Public Accountants, representing 30,000 CPAs in public practice, industry, government and education, welcomes the opportunity to comment on the above captioned exposure draft.

The NYSSCPA’s Auditing Standards Committee deliberated the exposure draft and prepared the attached comments. If you would like additional discussion with us, please contact Robert N. Waxman, Chair of the Auditing Standards Committee at (212) 755-3400, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,



Sharon Sabba Fierstein  
President

Attachment

**NEW YORK STATE SOCIETY OF  
CERTIFIED PUBLIC ACCOUNTANTS**

**PCAOB Release No. 2008-006  
COMMENTS ON PROPOSED AUDITING STANDARDS RELATED TO THE  
AUDITOR'S ASSESSMENT OF AND RESPONSE TO RISK  
(PCAOB Rulemaking Docket Matter No. 026)**

**February 18, 2009**

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# **New York State Society of Certified Public Accountants**

## **Auditing Standards Committee**

### **Comments on**

#### **PCAOB Release No. 2008-006 Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk**

The New York State Society of Certified Public Accountants welcomes the opportunity to comment on the PCAOB's *Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk* (the proposed standards).

We support the PCAOB's efforts to improve the risk assessment procedures undertaken during an audit. We generally agree with the provisions of the proposed standards; however, we have the following comments for your consideration. Our comments are organized such that our overall observations on the proposed standards are presented, followed by responses to the specific questions posed in the PCAOB release. Further, we have included additional comments related to specific proposed standards when the specific questions did not sufficiently address our comments.

### **OVERALL COMMENTS FOR CONSIDERATION**

#### **Organization of the PCAOB Standards**

We believe that the PCAOB standards should be structured so that all of the standards issued by the Board are consistent in style. For example, the proposed standards have objectives, while the existing standards do not. Additionally, some existing standards have terms defined in a separate "Glossary," some proposed standards have a "Definitions" section within the standard and other standards do not have any defined terms. The International Auditing and Assurance Standards Board (IAASB) and the AICPA Auditing Standards Board (ASB) are redrafting their auditing standards to promote greater clarity and more consistent application of their standards by auditors. We encourage the Board to undertake a similar project.

#### **Use of Terms "Must" and "Should"**

The use of the words "must" and "should" is not always consistent with their use in other PCAOB standards. For example, paragraph 9 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, states that "the auditor *should* [emphasis added] properly plan the audit of internal control over financial reporting and properly supervise any assistants," while paragraph 3 of the proposed standard *Audit Planning and Supervision* states "the auditor *must* [emphasis added] adequately plan the audit and properly supervise the members of the engagement team." We therefore recommend that the use of the terms "must" and

“should” in the proposed standards be reviewed to ensure that their use is appropriate and their meaning is clear.

### **Use of Objectives**

The PCAOB should consider how the objectives in the proposed standards are intended to be used. For example, according to paragraph 20 of International Standards on Auditing (ISA) 200 (Revised and Redrafted), *Overall Objectives of the Independent Auditor, and the Conduct of an Audit in Accordance with International Standards on Auditing*, the auditor should use the objectives in relevant ISAs to (a) determine whether any audit procedures in addition to those required by the ISAs are necessary to achieve the objectives stated in the ISAs, and (b) evaluate whether sufficient appropriate audit evidence has been obtained. We believe that the PCAOB should add objectives to all of its standards, and should provide a context for their use in a separate standard similar to ISA 200.

### **Standard Setting Process**

We support the PCAOB’s continued use of task forces with significant expertise to help compose drafts of auditing standards and we support the use of task forces in your efforts to obtain early public input from certain interested individuals or organizations prior to the formal public comment period. Early interaction with the public helps to achieve a more effective and efficient standard-setting process. We also support the continued participation of Board members and staff in joint task forces with the IAASB and the ASB. This participation aids the discussion and resolution of some of the more complex audit issues facing the Profession, and will help in reaching the goals of greater convergence of the Board’s standards with the ISAs and Statements on Auditing Standards (SASs).

### **Requirements versus Application Guidance**

In certain paragraphs of the proposed standards, we noted the ISA application guidance was elevated to requirements that we believe should be retained as guidance. Examples include:

- Paragraph 20 of the proposed standard, *Audit Planning and Supervision*, requires (through the use of the term “should”) the level of supervision to be appropriate for the circumstances and lists certain factors. Given this presumptive requirement which is attached to a list of factors, it is unclear what action is intended as a result of such a requirement. We suggest that a better structure would be to require the auditor to plan the nature, timing and extent of the direction and supervision of engagement team members, and, as application guidance, to provide factors that may impact supervision. This structure would be similar to paragraph A15 of ISA 300, *Planning an Audit of Financial Statements*, and be treated as application guidance.
- Paragraph 12 of the proposed standard, *Identifying and Assessing Risks of Material Misstatement*, seems to require the auditor to obtain an understanding of specific listed characteristics of the nature of a company. These same

characteristics, and others, are listed in the application guidance paragraphs A21-A22 of ISA 315, *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment*.

### **Fraud Guidance**

While we support the proposed standards' focus on the risk of fraud, we believe that the fraud guidance has been incorporated inappropriately in certain sections. For example, we believe that paragraph 13 of the proposed standard, *The Auditor's Responses to the Risks of Material Misstatements*, is redundant in that it requires the same procedures to address the risk of management override that are included in AU 316. We believe that the proposed standards should instead include references to other standards when necessary in order to eliminate the potential for inconsistencies or repetitiveness among different standards.

### **COMMENTS ON EACH OF THE PROPOSED STANDARDS**

#### ***Audit Risk in an Audit of Financial Statements:***

- 1. Does the proposed standard appropriately describe audit risk and its component risks?**

We believe that the proposed standard does appropriately describe audit risk and its component risks.

#### ***Audit Planning and Supervision:***

- 2. Is it reasonable and appropriate to extend the Auditing Standard No. 5 requirement regarding consideration of matters important to the audit of internal control over financial reporting to audits of financial statements?**

It is reasonable and appropriate to extend the Auditing Standard No. 5 requirement regarding consideration of matters important to the audit of internal control over financial reporting to audits of financial statements because the planning and risk assessment process is the same for an integrated audit as it is for an audit of financial statements.

- 3. Is the direction regarding multi-location engagements reasonable and appropriate?**

We believe that the direction regarding multi-location engagements is reasonable and appropriate.

- 4. Is more direction needed regarding multi-location engagements? If so, in what areas is additional direction needed?**

We do not believe that more direction is necessary regarding multi-location engagements.

**5. Are the responsibilities of the engagement partner for planning and supervision appropriate and reasonable, and is the proposed direction clear?**

ISA 300, *Planning an Audit of Financial Statements*, further describes the role of the engagement partner and other key members of the engagement team in paragraphs A5 and A9. The responsibilities of the engagement partner in the proposed standard could be further clarified if guidance similar to these paragraphs were included in the proposed standard.

***Additional Comments on Audit Planning and Supervision:***

We believe it is neither appropriate nor necessary for objectives in individual standards to contain the terms "must" or "should." Such words should be reserved for the requirements that support the objectives of the standards. Accordingly, we recommend that paragraph 3 of the proposed standard be moved from the "Objective of the Auditor" section of the proposal and incorporated as requirements under the "Planning an Audit" and "Supervision" sections of the proposed standards.

Paragraph 10 states, "the auditor should develop a written audit plan." However, the term "written" can be misleading in the age of electronic work paper documentation. As such, we recommend that the Board revise this paragraph to state, "The auditor should develop an audit plan, which should be documented electronically or in writing and should include a description of..."

We believe it would be helpful to auditors to include a footnote in paragraph 13 that references the extant guidance in AICPA Professional Standards, Volume 1, AU 336, *Using the Work of a Specialist*, to address the auditor's consideration of using individuals with specialized skills and knowledge. We further believe that such a footnote should include examples of specialists (other than Information Technology (IT) specialists) who might be necessary in conducting an audit or refer to examples of specialists who are listed in AU 336.

***Identifying and Assessing Risks of Material Misstatement:***

**6. Does the proposed standard clearly and adequately describe the auditor's responsibilities for performing risk assessment procedures?**

The proposed standard does clearly and adequately describe the auditor's responsibilities for performing risk assessment procedures.

**7. Are the additional procedures in paragraph 13 that the auditor should consider performing when obtaining an understanding of the company and its environment reasonable and appropriate for audits of issuers? Should**

**these procedures be specifically required for all audits, or is the responsibility to consider performing the procedures sufficient?**

The additional procedures are reasonable and appropriate. We agree that the requirement to consider performing the procedures is sufficient.

- 8. Is the new requirement to assess certain matters related to the control environment component of internal control over financial reporting reasonable and appropriate? Is the difference between the required performance for an audit of internal control over financial reporting and an audit of financial statements only clear?**

The requirement to assess certain matters related to the control environment component of internal control over financial reporting is reasonable and appropriate. Additionally, the difference between the required performance for an audit of internal control over financial reporting and an audit of financial statements only is clear.

- 9. Is the additional direction regarding the period-end reporting process reasonable and appropriate for audits of financial statements only?**

The additional direction is reasonable and appropriate.

- 10. Are the requirements and direction regarding the auditor's responsibilities for evaluating design and implementation of controls as part of obtaining an understanding of internal control over financial reporting sufficient and clear? If not, what additional direction is needed?**

The requirements and direction is sufficient and clear.

- 11. Does the additional description of the key engagement team members provide a better understanding of the expected participants in the discussion?**

The additional description of the key engagement team members does provide a better understanding of the expected participants in the discussion.

- 12. Does the discussion of significant risks in this standard provide sufficient direction to enable auditors to identify significant risks?**

The discussion of significant risks in this standard provides sufficient direction to enable auditors to identify significant risks.

- 13. Should the proposed standards include specific requirements and direction regarding documentation, e.g., summaries of the identified and assessed risks and the linkage to the auditor's responses?**

We do not believe the standards should include specific requirements and direction regarding documentation.

***The Auditor's Responses to the Risks of Material Misstatement:***

**14. Does the proposed standard clearly describe the auditor's responsibilities regarding tests of controls in integrated audits and in audits of financial statements only?**

The proposed standard does describe clearly the auditor's responsibilities regarding tests of controls.

**15. Are the requirements and direction regarding tests of controls appropriately aligned with Auditing Standard No. 5?**

The requirements and direction regarding tests of controls are appropriately aligned with Auditing Standard No. 5.

**16. Does the proposed standard clearly describe the auditor's responsibilities regarding substantive procedures?**

The proposed standard does describe clearly the auditor's responsibilities regarding substantive procedures.

***Additional Comments on The Auditor's Responses to the Risks of Material Misstatement:***

We believe paragraph 50 should be re-worded as follows: "If the auditor *discovers* misstatements that he or she did not expect when assessing the risks of material misstatements, the auditor...." We further believe that because of its importance, this paragraph should follow paragraph 41 (and that all subsequent paragraphs should be renumbered).

***Evaluating Audit Results:***

**17. Does the proposed standard clearly describe the auditor's responsibilities regarding the evaluation of audit results?**

The proposed standard describes clearly the auditor's responsibilities regarding the evaluation of audit results.

**18. Are the requirements and direction regarding the accumulated identified misstatements and evaluating uncorrected misstatements appropriate and adequate?**

The requirements and direction regarding accumulating identified misstatements and evaluating uncorrected misstatements are appropriate and adequate.

**19. Are the requirements and direction regarding the evaluation of the results of the integrated audit appropriately aligned with Auditing Standard No. 5?**

The requirements and direction regarding the evaluation of the results of the integrated audit in this proposed standard are appropriately aligned with Auditing Standard No. 5.

***Consideration of Materiality in Planning and Performing an Audit:***

**20. Are the requirements and direction in this standard appropriately aligned with the concept of materiality as described in the courts' interpretation of the federal securities laws?**

The requirements and direction in the proposed standard appear consistent with the courts' interpretation of the concept of materiality. Materiality should be based on the "users" of the financial statements and the proposed standard clearly indicates that the surrounding circumstances and the "users" of the financial statements should be considered when determining materiality.

**21. Does the proposed standard sufficiently and clearly describe the auditor's responsibilities regarding (a) establishing an appropriate materiality level for the financial statements as a whole and (b) establishing a lower materiality level or levels for particular accounts or disclosures? If not, what additional direction is needed?**

The proposed standard sufficiently and clearly describes the auditor's responsibilities regarding establishing appropriate materiality levels.

**22. Is the use of the term "tolerable misstatement" in the proposed standard appropriate and sufficiently clear?**

The use of the term "tolerable misstatement" is not sufficiently clear because the term is only referenced in paragraph 8 of the proposed standard to paragraph 18 of AU Sec. 350, *Audit Sampling*. The definition of "tolerable misstatement" should be clearly explained in this section and the reference to paragraph 18 of AU 350 should be removed.

***Additional Comments on Consideration of Materiality in Planning and Performing an Audit:***

In the note to paragraph 3, we believe that the last sentence, "However, it ordinarily is not practical to design audit procedures to detect misstatements that are material based solely

on qualitative factors” should be removed because we believe that it is practical to design audit procedures to detect material misstatements based solely on qualitative factors.

***Audit Evidence:***

**23. Does the proposed standard clearly describe the principles necessary for evaluating the sufficiency, relevance, and reliability of audit evidence?**

Certain paragraphs should describe more clearly the principles necessary for evaluating the sufficiency, relevance, and reliability of audit evidence. For example, the third bullet in paragraph 8 states, “Evidence obtained directly by the auditor is more reliable than evidence obtained indirectly.” The proposed standard does not explain the term “indirectly.” We believe the proposed standard should either clarify the term or provide examples of the types of evidence that are obtained indirectly.

Additionally, paragraph 29 of the proposed standards addresses situations in which inconsistent audit evidence is obtained or an auditor questions the reliability of audit evidence obtained. The guidance in paragraph 29 is inconsistent with the guidance in paragraph 9. For example, paragraph 29 directs the auditor to assess the effect, if any, on other aspects of the audit. Such guidance, however, is omitted from paragraph 9.

**24. Are the auditor’s responsibilities regarding the authentication of documents reasonable and appropriate?**

Paragraph 9 of the proposed standards addresses this issue and, in our opinion, needs additional guidance. We believe that if an auditor determines that “a document may not be authentic or that the terms in a document have been modified but that the modifications have not been disclosed to the auditor,” the auditor should follow the guidance in the auditing standards for the discovery of possible misstatements or illegal acts. We believe that the proposed guidance in this paragraph advising the auditor to “modify the planned audit procedures or perform additional audit procedures to respond to those conditions,” does not convey to an auditor the potential seriousness of this matter sufficiently and would not provide adequate guidance for the circumstances described.

**25. Are the requirements and direction related to selecting items for testing appropriate and clear?**

Additional guidance should be provided for addressing the selection process for the completeness assertion.

**26. Are the five categories of assertions in this standard sufficient or should they be expanded? If so, how would such expansion affect auditor performance?**

The Society believes that the proposed standard should be expanded to the 13 categories used in ISA 500, which are the same categories used by the AICPA, as they are more precise and complete. The five original categories do not adequately represent the assertions implicit in dynamic information (classes of transactions and events for the period) and in disclosures.

**Additional Comments on *Audit Evidence*:**

Paragraph 12 states the following:

*The auditor may base his or her work on assertions that differ from those in this standard if:*

- a. In the audit of financial statements, the assertions are sufficient for the auditor to identify the types of potential misstatements and appropriately respond to the risks of material misstatement in each significant account and disclosure that have a reasonable possibility of containing misstatements that would cause the financial statements to be materially misstated, and*
- b. If the audit is an integrated audit of the financial statements and internal control over financial reporting, the auditor has selected and tested controls over the pertinent risks in each significant account and disclosure that have a reasonable possibility of containing misstatements that would cause the financial statements to be materially misstated.*

The meaning of subparagraph b. is unclear. Specifically, this paragraph does not explain how testing controls as part of an integrated audit changes the nature of the relevant assertions. Subparagraph b. implies that assertions were indirectly addressed through control testing—not that they are different assertions. The intent of subparagraph b. should be clarified.