

December 11, 2014

Ms. Sherry Hazel
Audit and Attest Standards Team
AICPA
1211 Avenue of the Americas, 19th Floor
New York, NY 10036-8775

Re: September 10, 2014 ASB Exposure Draft of a Proposed Statement on Auditing Standards, *An Audit of Internal Control Over Financial Reporting That Is Integrated with an Audit of Financial Statements*

Dear Ms. Hazel:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to speak on behalf of local and regional firms and represent those firms' interests on professional issues in keeping with the public interest, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective.

TIC has reviewed the ED and is providing the following comments for your consideration.

GENERAL COMMENTS

TIC supports repositioning the extant standard on integrated audits (AT 501) from the attestation standards to the auditing standards. TIC believes the change is logical and would be consistent with the positioning of PCAOB Auditing Standard (AS) No. 5, *An Audit of Internal Control Over Financial Reporting That is Integrated with an Audit of Financial Statements*. TIC is also supportive of the Board's future plans to explore the development of an attestation standard that would address examinations of internal control, other than internal control over financial reporting (ICFR).

The remainder of this letter includes TIC's responses to the questions for respondents and other comments. A number of these comments note certain inconsistencies between this ED and the existing risk assessment standards, along with TIC's suggestions.

SPECIFIC COMMENTS

1. *Are respondents aware of any unintended consequences that would result from moving the content of extant AT section 501 from the attestation standards into GAAS?*

Yes, TIC believes an unintended consequence that could result from moving the content of extant AT section 501 into the SASs is the potential for inconsistencies between the ED and the clarified risk assessment standards. TIC found one such example in the guidance on walkthroughs.

Paragraph A54 of the ED includes a few explicit points as to what a walkthrough involves and how it is performed and suggests that “probing questions” may be effective as part of the auditor’s walkthrough procedures. However, the guidance provided in the ED is not repeated in AU-C 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*. Walkthroughs are only mentioned in passing (paragraphs AU-C 315.A13 and .A69.), with detailed guidance on this topic provided only in the AICPA Audit Guide, *Assessing and Responding to Audit Risk in a Financial Statement Audit* (the Guide), paragraphs 3.122-3.127 and 6.65-6.68.

Since walkthroughs are a common procedure in non-integrated audits of an entity’s financial statements, TIC believes it is important to have consistent guidance on this topic for both integrated and non-integrated audits, unless a reason exists for differences.

TIC recommends that the Board reconsider paragraphs A53-A54 of the ED and decide whether “probing questions” are an important element for walkthroughs of non-integrated audits. If so, the text of A53-A54 should be added to the Guide. If not, then the ED should be clarified to indicate that the “probing questions” are unique to integrated audits. Without such clarification, auditors may become confused as to the extent of the inquiries necessary for integrated v. nonintegrated audits.

The Other Comments section below presents other examples of potential inconsistencies between the ED and the clarified risk assessment standards.

2. *Do respondents agree with the approach the ASB has taken in proposing a separate standalone SAS instead of addressing an integrated audit in each relevant existing AU-C section?*

Yes, TIC agrees with the approach of having a separate standalone SAS because the majority of audits performed under GAAS are not integrated audits. The new SAS will provide a self-contained resource for the incremental guidance on integrated audits without cluttering up other SASs with guidance that may be irrelevant to the majority of auditors.

3. *Do the respondents agree with the approach the ASB has adopted relating to the 2013 COSO framework?*

Yes. TIC agrees that the same general approach is also appropriate for AU-C 315 and AU-C 330, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*. That is, each standard should presume that management

has used the 2013 COSO framework but should also allow for the use of other suitable frameworks if they meet the requisite criteria.

4. *Does the defined term significant class of transactions, account balance, or disclosure have the effect of better aligning terminology with minimal impact on practice?*

Yes, the definition should have minimal impact on current practice.

OTHER COMMENTS

Paragraph 9—The second sentence of this paragraph states:

If management refuses to furnish a written assertion despite its initial agreement to provide one, the auditor should withdraw from the engagement.

TIC believes this paragraph should be clarified to discuss those situations where the auditor is required to withdraw from the integrated audit due to management's refusal to furnish a written assertion but, for whatever reason, will continue with the audit of the basic financial statements. TIC recommends that the above sentence be amended, as follows:

...the auditor should withdraw from the ICFR engagement. [Emphasis added]

In addition, application material should be added to discuss the auditor's considerations and responsibilities with respect to the audit of the basic financial statements when management refuses to furnish a written assertion on ICFR.

Paragraphs A58 and A60—TIC noted inconsistencies in language between the ED and AU-C 315 and AU-C 330 regarding procedures performed to evaluate the design effectiveness and test the operating effectiveness of ICFR. Paragraphs A58 and A60 of the ED explain that evaluating design effectiveness or testing the operating effectiveness of a control may include:

a mix of inquiry of appropriate personnel, observation of the entity's operations and inspection of relevant documentation, recalculation, and reperformance of the control. [Emphasis added]

Although use of the phrase "observation of the entity's operations" is consistent with sentences in AS 5 (paragraphs 43 and 45) and AT 501.59, this phrase differs from the discussion of this topic in AU-C 315.A69 and AU-C 330.A28. AU-C 315.A69 talks about "observing the application of specific controls" when obtaining evidence about the design and implementation of relevant controls. AU-C 330.A28 does not mention either concept and offers only inspection, recalculation and reperformance as the procedures that would be performed in combination with inquiries of entity personnel when testing the operating effectiveness of controls.

TIC could not think of any reasons why the application guidance in this ED should differ from the application guidance in the general risk assessment standards. However, TIC believes that referring only to the entity's operations is too broad to be helpful and that the auditor is more likely to be focused on the observation of specific controls (as discussed in AU-C 315.A69).

TIC therefore recommends that the Board re-examine paragraphs A58 and A60 of this ED, along with AU-C 330.A28, to ensure that the guidance across these standards is consistent. TIC believes the best alternative for each standard is "observation of specific control activities." TIC also recommends adding the following phrase to paragraph A60:

Inquiry alone, however, is not sufficient for such purposes.

Paragraph A72—This paragraph provides guidance for testing control effectiveness in smaller, less complex entities that may have relatively informal documentation regarding the operation of their controls. In discussing the other procedures that could supplement inquiries of management, an example given is "observation of activities." Although this language is consistent with AS 5.51 and AT 501.71, TIC believes it is too general to be useful and should be changed to "observation of specific control activities." This alternative is consistent with our recommendation above and would also maintain consistency of language within the ED.

Paragraph A60—In addition to the edits suggested above, TIC also recommends that the guidance in paragraph A60 include a cross-reference to AU-C 330.A28+, which provides additional guidance on the mix of procedures (other than inquiry) that may be appropriate when testing the operating effectiveness of controls. TIC believes this cross-reference is necessary if the final integrated audit SAS will not provide detailed application guidance on these tests of controls.

Paragraph A79—When the auditor is updating control testing from an interim date to the entity's period end, paragraph A79 suggests that:

In some circumstances, such as when evaluation of [certain] factors indicates a low risk that the controls are no longer effective during the rollforward period, inquiry alone might be sufficient as a rollforward procedure.

TIC noted that paragraph A79 is inconsistent with AU-C 330.A36 and the Guide (paragraphs 3.114-3.115 and 6.22), which do not provide the same option to rely on inquiries alone as a rollforward procedure during the intervening period. As is, TIC believes confusion could occur as to whether the paragraph could be applied in the general risk assessment standards when performing a non-integrated audit. In addition, procedures for an integrated audit where the auditor will be opining on internal control over financial reporting should not appear to be more flexible than those for a non-integrated audit. To resolve the inconsistency, TIC recommends that paragraph A79 of the ED should be repeated in AU-C 330.A36 and the Guide.

EDITORIAL COMMENTS

Paragraphs 26 and A40—The ED contains an error message at the end of paragraph 26 in place of the usual cross-reference to the appropriate application paragraph. TIC believes paragraphs A38 through A40 would be the correct references.

Paragraph 44—The ED includes application guidance for this requirement; however, the requirement paragraph does not include a cross-reference to the application material. TIC recommends that a cross-reference to paragraphs A69 through A72 be added to the final standard.

Paragraph 84—TIC suggests removing the cross-reference to paragraph A121. It appears that the Board intended to delete this reference, since only paragraph A122 provides application guidance regarding paragraph 84.

Paragraph A43—The last sentence of this paragraph includes a cross-reference to paragraph A16. However, paragraph A16 does not seem relevant to control activities relevant to internal control over financial reporting. TIC recommends that this paragraph be reassessed to determine if a different paragraph was meant to represent the cross-reference.

Paragraph A53—The second sentence of this paragraph states:

A walkthrough involves following a transaction from origination through the entity's processes, including information systems, until it is reflected in the entity's financial records using the same documents and IT that entity personnel use.

TIC noted that the above sentence differs slightly from a similar sentence that appears in the Guide. Paragraph A53 refers to “financial records,” while paragraph 3.124 of the Guide refers to “financial statements.” TIC recommends that this inconsistency be resolved by changing the phrase in paragraph A53 from “financial records” to “financial statements.” TIC believes the wording in the ED should be conformed to the phrase used in the Guide because the auditor expresses an opinion on the financial statements, not the “financial records.”

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,



Scot Phillips, Chair
PCPS Technical Issues Committee

cc: PCPS Executive and Technical Issues Committees