

May 6, 2009

Ms. Sherry Hazel
AICPA
1211 Avenue of the Americas
New York, N.Y. 10036-8775

By e-mail: shazel@aicpa.org

Re: Proposed Statements on Auditing Standards – Risk Assessment

Dear Ms. Hazel:

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**

**COMMENTS ON
PROPOSED STATEMENTS ON AUDITING STANDARDS – RISK ASSESSMENT**

May 6, 2009

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New York State Society of Certified Public Accountants
Auditing Standards Committee

Comments on
Proposed Statements on Auditing Standards, *Risk Assessment*

The New York State Society of Certified Public Accountants welcomes the opportunity to comment on the AICPA Auditing Standards Board's (ASB) Proposed Statements on Auditing Standards, *Risk Assessment* (the proposed standards).

We support the ASB's efforts to improve the risk assessment procedures undertaken during an audit, and to converge the proposed standards with International Standards on Auditing (ISAs). 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 explanatory memorandum. Further, we have included additional comments for your consideration on certain proposed standards.

Overall Comments for Consideration

Convergence with ISAs

In certain instances, whole paragraphs from the ISAs were carried over to the proposed standard, but the cross-references within the proposed standards were not always updated. For example, paragraph A24 of the proposed standard, *Planning an Audit*, has the same paragraph references as the related ISA 300; however, the correct cross-references are paragraphs A13 and A22. As such, we recommend that the ASB review all of the proposed standards to ensure the internal cross-references are correct.

Guidance to be moved to other standards

In various proposed standards, certain guidance has been deleted from the standard in anticipation of inclusion in another standard that is often yet to be exposed. To ensure that all content that is proposed to be moved from one standard to another is appropriately tracked and to provide transparency to the process, we suggest aggregating all such movements and posting them to a tracking document on the ASB Clarity Project and Convergence portal. For example, we note that the following guidance is proposed to be included in other standards:

- In the "Comparison of Proposed SAS, *Materiality in Planning and Performing an Audit* (Redrafted) to ISA 320," the description in the comment column for paragraph 17 of the extant standard states, "Content should be covered by the proposed SAS, *Overall Objective*." However, we note that this standard was already exposed and the content from this paragraph was not included within that standard.

- We note that paragraphs 5 to 10 of extant AU section 311, *Planning and Supervision*, that address the auditor’s responsibilities about the early appointment of the independent auditor and establishing the terms of the engagement are to be included in the proposed SAS, *Terms of Engagements*. Additionally, paragraphs 28 to 32 of extant AU section 311 are to be moved to a yet to be proposed standard, *Quality Control for Audit Engagements*.
- We note that paragraphs 19 and 45 of extant AU section 314, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, are not included in the related proposed standard, since they are expected to be addressed in other standards.

Audits of smaller and less complex entities

Similar to the International Federation of Accountants’ (IFAC) project to develop implementation guidance in applying the ISAs for small and medium entities, we believe that the ASB should, in each of its proposed standards, either (a) state that there are no differences in audit procedures between larger entities and smaller, less complex entities, or (b) provide more robust guidance specific to smaller and less complex entities. Such guidance should preferably include specific examples of how audit procedures would differ for smaller and less complex entities.

Proposed SAS, *Audit Evidence* (Redrafted)

1. Is the auditor’s objective appropriate?

We believe the auditor’s objective is appropriate.

2. Are revisions from the existing standards to converge with the ISAs appropriate?

We believe that the revisions from the existing standards to converge with the ISAs are appropriate. As set out in the explanatory material, we agree with the proposed transfer of paragraphs 14 to 19 of AU section 326, relating to the auditor’s use of assertions in obtaining evidence, to AU section 314, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, that is consistent with ISA 500, *Audit Evidence*.

3. Are the differences between the proposed SASs and the ISAs, identified in exhibit A, and other language changes, appropriate?

We believe that the differences between the proposed SASs and the ISAs, and other language changes, are generally appropriate. We support the development of a separate SAS that focuses on the specific circumstances in which an auditor uses the work of management’s specialist. As such, we agree with omitting ISA 500, paragraph 8(c) from the proposed standard. Additionally, we believe that

information produced by management's specialists would also be subject to paragraph 8(b), which refers to "evaluating whether the information is sufficiently precise and detailed for purposes of the audit." Accordingly, we recommend that the phrase "including any management's specialist" be included in paragraph 8, as follows:

When using information produced by the entity, *including any management's specialist*, the auditor should evaluate whether the information is sufficiently reliable for the purposes of the audit...

Further, we note that the reference to the use of information prepared by management's expert has not been carried forward from paragraph A1 of ISA 500 to paragraph A1 of the proposed standard. While we support the development of a separate standard on the use of management's specialists, we suggest retaining the reference to management's specialists in paragraph A1, with the addition of a note referencing the new standard on using the work of management's specialists.

Additional Comments:

In the definition of sufficiency (of audit evidence) in paragraph 5, we believe that the quantity of audit evidence needed may also be affected by the type of sampling method selected.

We note that the application guidance in paragraph A18 of the proposed standard, relating to external confirmations, does not reflect the PCAOB's April 14, 2009 concept release on possible Revisions to the PCAOB's standard on audit confirmations. To facilitate an effective dialogue regarding confirmations used as audit evidence and the process of obtaining confirmations, we recommend that the ASB coordinate its efforts with the PCAOB to develop a single set of high quality standards relating to the confirmation process.

In addition, we believe the following edits to paragraph A18 would provide improved clarity to reflect the various means of obtaining confirmations, including the use of electronic requests or responses (additions are shown in italics and deletions as strikethrough text):

An external confirmation represents audit evidence obtained by the auditor as a direct ~~written~~ response to the auditor from a third party (the confirming party) in paper form, or by electronic or other medium. External confirmation procedures are used frequently in relation to account balances and their constituent parts. For example, the auditor ~~may~~ *is usually required to* seek direct confirmation of receivables by communication with ~~debtors~~ *customers*. However, external confirmations ~~need not be restricted to these items. For example, the auditor may request~~ *may also be appropriate in other circumstances, such as requesting* confirmation of the terms of agreements or transactions an entity has with third parties; ~~the~~

~~confirmation request is designed to ask, or confirming~~ if any modifications have been made to the agreements and, if so, what the relevant details are. External confirmation procedures also are used to obtain audit evidence about the absence of certain conditions, for example, the absence of a “side agreement” that may influence revenue recognition. See AU Section 330, The Confirmation Process (AICPA, Professional Standards, vol. 1) for further guidance.

We believe that the fifth bullet point of paragraph A32 can be further clarified by revising the sentence into two separate and distinct points, as follows:

Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies, facsimiles, or documents that have been filmed, digitized, or otherwise transformed into electronic form. *Furthermore*, the reliability of ~~which~~ photocopies, facsimiles, or documents that have been filmed, digitized, or otherwise transformed into electronic form may depend on the controls over their preparation and maintenance.

We believe that the last sentence of paragraph A35 should be revised as follows:

Similarly, if the auditor intends to test a population (for example, payments) for a certain characteristic (for example, authorization), the results of the test will be less reliable if the population from which items are selected for testing is not complete, *or if the population includes items for which the characteristic is not relevant.*

Proposed SAS, *Materiality in Planning and Performing an Audit* (Redrafted)

1. Is the auditor’s objective appropriate?

We believe the auditor’s objective is appropriate.

2. Are revisions from the existing standards to converge with the ISAs appropriate?

Overall, we believe the revisions from the existing standards to converge with the ISAs are appropriate, and we support the division of extant AU section 312, *Audit Risk and Materiality in Conducting an Audit*, into two separate standards, consistent with the formulation of the ISAs. Additionally, we support moving the definition of audit risk and its components to the proposed SAS, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Generally Accepted Auditing Standards*.

However, we suggest revising the first two sentences of paragraph 6, as follows, to clarify that the judgments the auditor makes about the size of misstatements

that will be considered material to the financial statements also provides a basis for establishing a limit on untested populations:

In planning the audit, the auditor makes judgments about the size of misstatements that will be considered material *to the financial statements*. These judgments provide a basis for:

- (a) determining the nature, timing, and extent of risk assessment procedures;
- (b) identifying and assessing the risks of material misstatement;
- (c) determining the nature, timing and extent of further audit procedures;
- (d) *establishing a limit on untested populations*.

Additionally, we believe that the meaning of paragraph A14 is unclear, and does not provide sufficient guidance regarding performance materiality, as mentioned in paragraph 11. We propose that the ASB revisit the guidance provided in paragraph A14, and revise this paragraph to provide further clarification. In particular, we suggest that further explanatory and application guidance be added to paragraph A14 with respect to materiality taken as a whole and materiality determined for a particular class of transactions, account balance, or disclosure. Finally, we believe that paragraph A14 should be congruent with the proposed SAS, *Audit Sampling (Redrafted)*.

3. Are the differences between the proposed SASs and the ISAs, identified in exhibit A, and other language changes, appropriate?

We note that paragraph A7 is derived from paragraph 30 of extant AU section 312, and that this guidance is not included within ISA 320. While we understand the reason to retain this guidance, we believe that it should provide a clearer link to the requirement in paragraph 10 of the proposed standard by adding the following:

While user expectations may differ based on inherent uncertainty associated with the measurement of particular items in the financial statements, this factor has already been considered in the auditor's determination of materiality, and would not cause the auditor to follow different procedures for planning or evaluating misstatements than those outlined for other entities.

Proposed SAS, *Evaluation of Misstatements Identified during the Audit*

1. Is the auditor's objective appropriate?

We believe the auditor's objective is appropriate.

2. Are revisions from the existing standards to converge with the ISAs appropriate?

As noted in the supplementary material, paragraphs 62 to 67 of extant AU section 312, which address the auditor's responsibilities to evaluate the overall effect of audit findings on the auditor's report, are expected to be included within AU section 508, *Audit Reports*. While some of this guidance is applicable to forming an opinion, we believe that certain guidance would be more appropriate within the proposed SAS, *Evaluation of Misstatements Identified during the Audit*. For example, the guidance in extant AU section 312, paragraph 63, which provides guidance on the factors to consider when concluding whether the effect of misstatements are material, seems more appropriately placed in this proposed SAS rather than in AU section 508. We recommend that the ASB reconsider the placement of the guidance in each of these paragraphs.

3. Are the differences between the proposed SASs and the ISAs, identified in exhibit A, and other language changes, appropriate?

We believe that the differences between the proposed SASs and the ISAs, and other language changes, are appropriate. However, see our other proposed revisions below in "Additional Comments."

Additional Comments:

We suggest the following revision to paragraph 8 of the proposed standard:

If, at the auditor's request, management has examined a class of transactions, account balance, or disclosure and corrected misstatements that were detected, the auditor should perform additional audit procedures, as ~~necessary~~ *appropriate in the circumstances*, to determine whether misstatements remain.

Proposed SAS, *Planning an Audit (Redrafted)*

1. Is the auditor's objective appropriate?

We believe the auditor's objective is appropriate.

2. Are revisions from the existing standards to converge with the ISAs appropriate?

The first sentence of paragraph 4 of the extant standard permits the auditor with final responsibility for the audit to delegate portions of audit planning to other firm personnel; however, we note that this concept was not carried forward to the redrafted standard. We do not believe that the proposed redrafting intended to change this practice, and as such, we suggest retaining this guidance in the proposed standard to avoid confusion that may occur as a result of its omission.

3. Are the differences between the proposed SASs and the ISAs, identified in exhibit A, and other language changes, appropriate?

We recommend that the ASB consider moving the procedures regarding initial audit engagements in paragraph A25 to a new proposed standard that follows the procedures outlined in ISA 510 (Redrafted), *Initial Audit Engagements – Opening Balances*.

Additional Comments:

In Exhibit B to the proposed standards, *Summary of Differences Between the PCAOB’s and the ASB’s Proposed Risk Assessment Standards*, the third bullet of Appendix 2 refers to the related PCAOB standard that addresses multilocation audits. We note that this topic is not included within the proposed standard, *Planning an Audit*; however, we believe that the ASB should re-consider including in this proposed standard guidance that relates to multilocation audits outside the group audit scenario.

Proposed SAS, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement (Redrafted)*

1. Is the auditor’s objective appropriate?

We believe the auditor’s objective is appropriate.

2. Are revisions from the existing standards to converge with the ISAs appropriate?

We believe that the revisions from the existing standards to converge with the ISAs are appropriate.

3. Are the differences between the proposed SASs and the ISAs, identified in exhibit A, and other language changes, appropriate?

We believe that the differences between the proposed SASs and the ISAs and other language changes, are appropriate. However, see our other proposed revisions below in “Additional Comments.”

Additional Comments:

Paragraph A109 states that “identifying relevant assertions includes determining the source of likely potential misstatements,” which does not take into account the concept of the materiality of the potential misstatement. We believe that this paragraph should be revised to instead focus the auditor’s attention on those relevant assertions that have a reasonable possibility of containing a material misstatement.

Paragraphs A121 and A122 of the proposed standard seem redundant, in that they both address risks relating to significant non-routine or judgmental matters. As such, we recommend that these paragraphs be combined into one integrated paragraph.

Paragraph A124 of the proposed standard provides guidance regarding the auditor's responsibility when management has not appropriately responded by implementing controls over significant risks. As currently stated, the guidance does not use the term "should" and instead uses the phrase "is required" in the application guidance. However, when the auditor has determined that at a minimum there is a significant deficiency, the auditor cannot disregard the implications of such a finding on his or her risk assessment. As such, we recommend revising paragraph A124 as follows:

If management has not appropriately responded by implementing controls over significant risks and if as a result the auditor judges that a significant deficiency exists or material weakness exists in the entity's internal control over financial reporting, the auditor ~~is required to~~ *should* communicate this matter to those charged with governance, ~~and in these circumstances, the auditor also may~~ consider the implications for the auditor's risk assessment.

Proposed SAS, Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained (Redrafted)

1. Is the auditor's objective appropriate?

We believe the auditor's objective is appropriate.

2. Are revisions from the existing standards to converge with the ISAs appropriate?

We believe that the revisions from the existing standards to converge with the ISAs are appropriate.

3. Are the differences between the proposed SASs and the ISAs, identified in exhibit A, and other language changes, appropriate?

Paragraph A17 has been revised from paragraph A15 of the ISA equivalent, ISA 330, by replacing the word "is" with "may be." However, we propose revising the second sentence of this paragraph as follows:

When a single purpose is met by a combination of procedures, the extent of each procedure ~~may be~~ *should be* considered separately.

Additional Comments:

The second sentence in the last part of paragraph A38 includes extraneous words that we suggest removing, so that the sentence reads as follows:

“If the rate of expected deviation is ~~to be~~ too high, tests of controls....”

We recommend that paragraphs 7(a)(ii) and A56 use the phrase “takes into account,” rather than “takes account of.”