

Via e-mail: comments@pcaobus.org

Nov 26th, 2013

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 2006-2803

Re: PCAOB Rulemaking Docket Matter No. 034: Proposed Auditing Standards on Auditor's Report and Auditor's Responsibilities Regarding Other information – The Required communication of Critical Audit Matters

Dear Members and Staff of the Public Company Accounting Oversight Board:

I appreciate the opportunity to comment on PCAOB's Proposed Auditor Reporting . As a member of the financial community and a investor, I support the proposed standards because they are intended to increase the informational value of the auditor's report and thus to promote its usefulness and relevance to investors and other financial statement users. While, I also want to express my concerns regarding the use of the new information, such as "critical audit matters", and the economic considerations entailing the proposed standards, especially the potential cost.

Basically, the type of auditor's report in the United States has been commonly described as a pass/fail model. The existing model seems to be useful since it states a straightforward and clear position on whether the financial statements are fairly presented (pass) or not (fail). However, the existing Auditor's report provides little, if any, information specific to a particular audit. Admittedly, the existing Auditor's report provides discussion and analysis for each significant financial statement account with some degree of detailed breakdown and necessary disclosure. But it fails to communicate with investors the considerations on specific accounts in terms of auditor's subjective judgment and evidence gathering, or

the influence and weights of matters in issuing Auditor's final opinion. Thus, the existing auditor's report is not informative enough for investors to make investment decision.

The proposed Auditor Reporting Standard would require the auditor to communicate in the auditor's report "critical audit matters", which could help to alleviate the information asymmetry that exists between company management and investors. Because company management is usually aware of the auditor's most challenging areas in the audit due to regular interactions with the auditor as part of the audit. However, investors do not usually know this information. When investors have a better grasp of the company's business, risk and material accounting issues, company would allocate the capital more efficiently and could lower the average cost of capital when investors have a better understanding of the company's business and risks.

The following are some examples of "critical audit matters" that could be communicated in the auditor's report under the proposed auditor reporting standard and that would be the additional information investor's are interested in obtaining.

- Areas of high financial statement and audit risk. For instance, a deficiency in internal control over financial reporting.
- Areas of significant auditor judgment. For instance, company's loss contingency, or going concern assumption
- Significant management judgments, estimates, and areas with significant measurement uncertainty, and application of accounting policy
- Significant changes or events affecting the financial statements, including unusual transactions; or incurrence of restatement.

To apply the proposed auditing standards regarding the “critical audit matters” to the practice of Auditor’s report, I analyzed the Diamond Food’s annual report as of and for the fiscal year ended July 31, 2010 and other relevant information concerning the company’s financial reporting to prepare a “critical audit matters” section. The format complies with the Board’s recommendations by including the identification of critical audit matters in the annual financial statement and related notes, considerations that led to determine the matter as critical, and relevant financial statement accounts and disclosure. There are two specific critical audit matters regarding Diamond Foods’s financial statements and other significant information, which are: 1) Company’s internal control over financial reporting, as of and for fiscal year ended on July 31, 2010 which was four month after its acquisition of Kettle Foods, and 2) Company’s estimation of Cost of Goods Sold and Account Payable after its restatement of financial statement for fiscal year 2010 and 2011.

The following comments primarily reflect my understanding and limited analysis are in response to certain questions set forth in the Proposed Auditing Standards.

10. Would the auditor's communication of critical audit matters be relevant and useful to investors and other financial statement users? If not, what other alternatives should the Board consider?

Yes. The proposed communication of "critical audit matters" section in the auditor’s report would be tailor-made to be specific for each financial statement audit by the auditor. By focusing on the areas involving high financial statement and audit risk and significant management and auditor judgment, the communication of “critical audit matters” would serve as the bridge for the gap of information that company’s management knows or auditor obtains during the audit while is unknown to investors. If these information is not sufficiently relevant and useful in terms of meeting investor’s need, the

Auditor Discussion & Analysis, required and expanded emphasis paragraphs or auditor assurance on other information outside would provide with additional information.

11. What benefits or unintended consequences would be associated with the auditor's communication of critical audit matters?

Undoubtedly, investors would benefit from additional auditor reporting and further unique and relevant insight obtained by the auditor during the audit of financial statements. Communicating “critical audit matters” would provide investors and other financial statement users with previously unknown information about the audit that could enable them to analyze more closely any related financial statement accounts and disclosures. Essentially, the required communication of “critical audit matters” would have two direct positive impact on investors, one is that it could direct investors’ attention on challenges associated with the audit that may contribute to the information used in their investment decision making; another one is that it could let investors focus on aspects of the financial statement that the auditor also found to be challenging.

To meet the proposed auditing standards requirement, auditor may change or adjust how they plan the audit procedure, obtain reliable evidence, present and disclose information and express their opinion, which would have an indirect positive impact on investors and other financial statement users. Since the auditor's new focus on and communication of critical audit matters could lead to improved financial statement disclosures related to areas that gave rise to critical audit matters in the first place. The potential improvement in the related financial statement disclosures could incrementally increase the quality of the information in the financial statements, which assist the investors in investment decision-making and better evaluating the company’s financial position, results of operations, internal control environment and cash flow.

13. *Could the additional time incurred regarding critical audit matters have an effect on the quality of the audit of the financial statements? What kind of an effect on quality of the audit can it have?*

Yes. On one side, the quality of the audit of the financial statement could be improved because auditor would focus on areas where ‘critical audit matters’ gave rise to offer deeper insight. On the other side, due to the staffing constraint and tight deadline, auditor may compromise some of its work in areas less material. The tradeoff may lead to the ignorance of potential risk of omission or misstatement. I expect that the incremental cost in terms of time and effort for auditor would be modest since auditor could leverage the audit works that have already required to be performed under the existing standards. And the “critical audit matters” could have already been addressed by auditor in forming the opinion on the financial statements.

22. *What are the additional costs, including indirect costs, or other considerations for companies, including their audit committees, related to critical audit matters that the Board should take into account? Are these costs or other considerations the same for audits of both large and small companies?*

Responding to the requirement of communicating “critical audit matters” in the auditor’s report, companies, including audit committee, would incur additional cost related to management review of and discussion with auditor about the “critical audit matters”. Although it’s auditor who determine, document and communicate the “critical audit matters” to the investors via auditor’s report, it’s actually the company’s responsibility of addressing the potential issues and material concerns. These costs or other considerations could be different for audits of large and small companies. For instance, small company may not have audit committee and need to set up a special committee to work with auditor for the proposed standards. While, large companies have audit committee which already has resource and personnel.

There are concerns about the use of the “critical audit matters” from investor’s perspective. The proposed communication in the auditor’s report could be something investors and other financial statement users not accustomed to review or analyze. The “critical audit matters” section could be misleading because it may deliver a wrong impression that all of the information important to investment decisions already highlighted as a critical audit matter, or investors may not understand the meaning of the critical audit matters correctly. Investors may seek guidance on the interpretation of a certain critical audit matter in the context of specific industry or company. It will be a good resource for investors to turn to if PCAOB could come up with a list of potential “critical audit matters” for reference.

In sum, the proposed communication of “critical audit matters” in the auditor’s report is intended to make the auditor’s report more informative and commutatively valuable to enhance its relevance and usefulness to investors and other financial statement users. The substantial benefits of the increased quality of corporate financial reporting and increased value of the auditor’s report to investors would outweigh the potential cost increase for auditor and company related to the proposed auditing standards.

I appreciate the opportunity to share my viewpoints on the Proposed Standards. If the Public Company Accounting Oversight Board has any questions regarding my comments, please contact me at az318@georgetown.edu.

Sincerely,

Emily Zhang