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Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 034

To the Members of the PCAOB,

I appreciate the opportunity to comment on the reproposed standard, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*. It has been a long, slow road to improving the audit report since the Board shouldered this load in 2011. I applaud the Board for taking on this unpopular task - one where the status quo is considered good enough by the preparer and auditor community; understandably so, because they are the ones who have the most work ahead of them if this becomes an auditing standard. Their main concern is the critical audit matters – the CAMs. It is my main concern as well.

While I understand the anxiety surrounding CAM reporting, I believe it is misplaced: The Board has dramatically slimmed down its proposal from the last iteration. The requirement that reported CAMs relate to material reporting matters of which the audit committee should be aware and involving significant auditor judgment should cause only the most important issues to be reported; there should be no unreasonably lengthy audit reports resulting from this requirement. I believe that the specter of oversized, boilerplate audit reports is being invoked in order to arouse opposition to the proposal, as well as the possibility that auditors might disclose information that might not be required to be disclosed by accounting standards. I do not believe that this is what the Board intends in the proposal, nor do I believe that auditors would want to interpret the proposed standard in that fashion.

Some critics charge that investors do not need this information because it is already handled by the auditors in their dealings with the audit committee of the board of directors. Both auditors and audit committee members are agents of the shareholders, and are supposed to be championing the interests of their principals. That's true, but are the agents really putting the interests of the principals first if they can't share the most critical issues with those principals?

Keep in mind that both auditors and board members – including audit committee members – are elected by the shareholders and the cost of retaining both sets of agents is borne by the shareholders. What would happen to most of us if we refused to tell our employers what they wanted to know about the way we did our jobs for them?

The question has been raised, even at the Board level: how will investors use the information in the CAMs? The question seems to be posed as a reason for not improving the audit report. The thinking may be that if investors won't use the information to say, fashion their quarterly or annual earnings estimates, then the information must not be worth the effort to collect it.

Before answering the question "how will investors use CAM information," I have a question of my own: how do investors use the audit report *now*? In thirty-plus years of working in the investment research world, I've rarely encountered anyone who reads them – and when they do read them, it's not for the purpose of incorporating nuggets of information from them into an earnings model.

Also before answering the question, let us also be clear on just who the term "investors" addresses. If one presumes the kind of investors typically showing up at shareholder meetings – that is, usually individual investors, rarely professional or institutional investors – the answer is that they'll probably do nothing with the information, and they very likely don't ever do anything at all with the audit report or the financial statements. Does that make the PCAOB's proposal a bad idea because this particular class of investors won't use the information? No. Should standard setting efforts be aimed at pleasing this particular segment of investors? No. If they're not going to use financial statements anyway, it's wrong to make financial reporting standards tailored to suit people who don't use financial statements. It's a waste of resources.

If, by investors, one means professional investors, that's still not a monolithic class. Some professional investors can go through their whole career without looking at audit reports or financial statements, and still function viably. Consider stockbrokers: it's unusual to encounter ones that will spend time with an annual report, but nevertheless, they can be considered investors. They will, however, have their opinions shaped by the advice of their firm's research analysts – and those are investors who are very likely to read financial statements and audit reports (especially if they believe the audit reports aren't in the category of "seen one, seen them all.") Also likely to read financial statements and audit reports are the in-house analysts of buy-side institutions like mutual funds – and they often invest on behalf of the individual investors who will never read financial statements or audit reports.

That category of investors – the professional, institutional investor – is the one that's likely to use the information resulting from the PCAOB's proposal. So, back to the question – how will these investors use the information in the CAMs?

They'll use it like they use any other information about accounting standards. They'll read it and form opinions when they understand it. Nobody questions how investors use accounting policy footnotes or critical accounting estimates. Those disclosures help investors get an idea of a firm's reporting environment, and they also help an investor get an idea of their own limits: for example, if a company has an accounting policy related to revenue recognition tied to multiple-element arrangements, and the investor has no idea what that means, it will be incumbent upon the investor to learn about them. These disclosures in the audit report will augment and add another dimension to the story told by accounting policy footnotes in the financial statements and the critical accounting policies and estimates disclosed in the Management's Discussion & Analysis – and because it comes from the auditor, who is very directly the agent of the investor, it should be valued very highly by investors.

What preparers and auditors fail to take into account is the fact that the level of accounting knowledge within the investor community is not always deep, and certainly not consistent among investor factions. Information can always be ignored and sometimes, investors choose ignorance when it comes to existing information about accounting policies or critical accounting estimates. Standard setters have not chosen to penalize investors who make good use of such information because some investors choose ignorance.

Unlike investors, auditors are experts in accounting matters, and they should be. If a firm's auditors find that a material matter was particularly taxing of their own judgment, and they communicated that fact to the audit committee - the other agents of the investors – then including it in the audit report would amplify the investors' own understanding of the other information in the financial statements about accounting policies and estimates. Hopefully, an investor might think that if an expert considered this to be a tough matter, then maybe it would make sense for the investor to really understand the issue well.

Not every disclosure or number in the financial statement package is “used” by investors in, say, building earnings estimates. They don’t “do” something with every figure in the package. That doesn’t mean information of a qualitative nature, such as the CAMs, is without its uses. If investors get into the habit of understanding them, they may find that there are other parts of the financial statement package they’ve been neglecting. Critics of the proposal may say there isn’t value to CAMs because investors won’t “do” something with them, but if CAMs exist in the audit report and investors read about them, they will add a useful element to the current reporting package: an expert’s link to the more vexing accounting issues embedded in the financial statement package. That will do more to highlight for investors the critical accounting issues of a company than any mere litany of accounting policies.

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If you have any questions about these thoughts, members of the Board or the staff are welcome to contact me to discuss further. Best regards.

Sincerely,

Jack Ciesielski