



PCAOB'S STAFF CONSULTATION PAPER: *AUDITING ACCOUNTING ESTIMATES AND FAIR VALUE MEASUREMENTS*

ICAEW welcomes the opportunity to comment on the PCAOB's Staff Consultation Paper: *Auditing Accounting Estimates and Fair Value Measurements* published by the PCAOB on 19 August 2014, a copy of which is available from this [link](#).

This ICAEW response of 3 November 2014 reflects consultation with ICAEW's Technical and Practical Auditing Committee and its PCAOB Panel.

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MAJOR POINTS

Support for the CP

1. We support the objectives of this Consultation Paper (CP) which will stimulate debate on the challenges associated with the audit of estimates and fair values, and this paper will stimulate debate. The general thrust of the paper is to introduce more specific requirements to auditing standards. While this might make some auditors spend more time on these issues, we think that any new standard would stand more chance of dealing with the issues effectively and thereby improve investor confidence, if auditors were more confident in their ability to tackle the issues, and were actively encouraged to challenge management, more assertively than they do now.

Acknowledging the wide range of issues affecting the audit of estimates and fair values

2. There are a number of widely acknowledged problems associated with the audit of estimates and fair values. Complex accounting issues and mathematical models used in the valuation of some financial instruments, a lack of available audit evidence and the lack of widely available expertise in these matters all affect auditors but, critically, they are largely beyond the control of auditors. That said auditors can and should be encouraged, through auditing standards, to challenge management, third parties and specialists, more than they do now, on a number of different levels.

Recognising the need for competence

3. Taking estimates and fair values at face value and simply seeking corroborative evidence to support management's assertions, without challenging them, is not acceptable. But dealing with a lack of auditor confidence, and a lack of auditor ability or willingness to challenge, cannot be achieved simply by setting out in detail the questions auditors should ask and what they should do in any given set of circumstances. The people who develop and promote the complex estimates and fair values embedded in some financial instruments are highly qualified, highly paid and sophisticated. The models on which such instruments are based are often technically complex. An effective audit requires auditors with the experience, competence and time budgets to effectively challenge the bases of calculation. Auditors need to understand the answers to the questions they ask about the methodologies applied. At present, auditors do not always have the necessary combination of qualities and resources.

The value of international harmonisation

4. We fully support the consolidation of the audit requirements for estimates and fair values into a single standard, consistent with ISAs, partly because of the similarities between estimates and fair values and partly because harmonisation is a worthy objective of benefit to US investors. The PCAOB should seek to build on the good (and often difficult) work performed by IAASB in this area in recent years. However, it is essential to recognise that despite the similarities, there are some specific aspects of the audit of fair values that are peculiar to that area, and are not relevant to the audit of the generality of estimates. IAASB's ability to bring these two areas together under one umbrella rested on the principles-based framework within which ISAs are developed. ISA 540 is also buttressed with non-mandatory guidance in IAPN 1000. Merging the two standards is not cost-free and includes permitting auditors to exercise judgement.

Challenging the basis on which estimates are developed, including the associated controls

5. Many restatements involve estimates and fair values, and many internal control deficiencies reported by auditors are those that have already been reported to them. If auditors are to report on other internal control deficiencies, they need the competencies and resources to challenge management and third parties regarding controls over estimate development processes. Auditor resources include auditing standards that permit and encourage them to exercise judgement. The word 'challenge', in the context of challenging management, does not appear in the CP at all. Encouraging challenge, the exercise of scepticism and the application of existing standards in the spirit in which they were intended might reduce the need for radical

changes to standards. In any case, the opportunity should be taken to reinforce the importance of challenge and scepticism. The PCAOB might consider using material from Staff Audit Alert Practice Alert No. 10 on professional scepticism in this context. Preparers and auditors should be encouraged to recognise their responsibilities for the development and audit respectively of estimates and fair values, especially where third parties are involved. These *responsibilities* cannot be outsourced or delegated.

6. The CP proposes a number of specific requirements. We believe that many of these would be better expressed as guidance on how to apply the main principles, rather than as explicit requirements. In a number of cases, we suggest that it would be better either for guidance material to be developed, or for any requirement to be for auditors to consider whether the performance of a number of different procedures, from a list of possible procedures, is appropriate in the circumstances. The CP proposes a presumption that certain estimates are significant risks, and that procedures are introduced to address specific standards, such as the revenue recognition standard. We do not think that either of these proposed requirements is likely to improve audit quality. Nevertheless, if the PCAOB decides that some specific guidance is needed regarding the identification of significant risks, we believe that a *rebuttable* presumption that certain risks are significant would be better. The onus would be on auditors to show that the risk is not significant and would mean that in cases in which the risk was not in fact significant, work would not be performed for compliance purposes only. Such work is not cost-free¹.

Imposing process requirements in the audit of fair values on the generality of estimates

7. Specific aspects of the audit of fair values that are peculiar to that area include the fact that the audit of fair values, particularly the audit of complex financial instruments, is often more process-driven than the audit of other estimates. At the same time, developing and auditing fair values often involve a high-level of judgement and the expertise required to exercise it. The overall impression given by this CP is that the process requirements surrounding fair values are being imposed on estimates generally. Furthermore, in our view, adding to current requirements in an attempt to make sure that there is less scope for abuse, and making all of it mandatory raises the bar, but without clear benefits. There is a risk that the outcome will be ever-lengthier checklists that will not serve to improve the quality of accounting estimates or the audit thereof, or enhance auditor scepticism.

Encouraging innovation

8. Innovation in audit is desired by regulators and firms alike, but it too comes at a price. Innovation requires judgement and judgement always involves the risk of misjudgement. If the risk of misjudgement is to be avoided at all costs, there can be no innovation. The audit of estimates in general and fair values in particular, is a minefield. There will always be developments that regulators will not have considered when issuing standards. A higher-level standard with fewer but tougher requirements, and more non-mandatory guidance material, would more readily accommodate innovation in audit.

Specialists engaged by companies and other third party sources

9. There are widely acknowledged problems with the independence of some specialists engaged by companies and of other third party valuation sources. There are often simply too few to go around. There are also widely acknowledged problems with the availability of external evidence to support their valuations. Specialists and other third parties often use proprietary information or methodologies that they are unwilling to release to auditors. The proposals for auditors to look for evidence from other third party sources and evaluate whether a

¹ The PCAOB proposed a rebuttable presumption to the effect that if audit work was not documented, the presumption would be that it had not been performed when its exposed Auditing Standard No 3 on audit documentation for comment back in 2004. Commentators, including ICAEW opposed that presumption and it was withdrawn, but the opposition was to substance of the rebuttable presumption, not rebuttable presumptions *per se*. The rebuttable presumption of fraud risk in revenue recognition has been in operation for some time in ISA 240 on fraud. Rebuttable presumptions are also used in IFRS.

methodology is accepted in a particular industry are impractical in the all too common cases in which there are no other third party sources of information about bespoke products, or where any such sources are unwilling or unable to provide the relevant information. The proposals to treat valuations from specialists and other third parties as if they were generated by the company itself simply ignore the issues. We are concerned that if these proposals are developed, they will create confusion by blurring the responsibilities of management and auditors, and that they will effectively require auditors to form judgements on the basis of non-existent or unobtainable evidence. A broad debate involving a number of stakeholders is needed regarding how such valuations should be audited.

Achieving the objective of the CP

10. We strongly suggest that in order to achieve the objectives of the CP:

- auditors should be encouraged to challenge management and third parties, rather than simply seeking corroborative evidence supporting management's assertions;
- the PCAOB acknowledge, and open a dialogue concerning the structural issues relating to
 - the competencies and resources of auditors in the face of highly qualified and remunerated specialists when dealing with complex valuation models;
 - the difficulties associated with the development of complex accounting estimates and fair values, and in particular the internal control and evidential issues;
 - the need to find a way for auditing standards to encourage rather than stifle innovation.

ANSWERS TO SPECIFIC QUESTIONS

Current requirements and practices

Q1. Does the information presented above reflect aspects of current audit practice? Are there additional aspects of current practice, of both larger and smaller audit firms – including centralized testing, the use of third parties, or specific challenges to auditing accounting estimates and fair value measurements – that are relevant to the staff's consideration of the need for standard setting in this area?

Q2. The staff understands differences may exist in the use of centralized or national-level pricing desks at audit firms. The staff is interested in current practice for interaction between national-level pricing desks and engagement teams. For example, how (and by whom) are national-level pricing desks supervised given the engagement partner's responsibility under the risk assessment standards? How should these considerations affect auditing standards?

Q3. What other issues relevant to the need for standard setting should be considered by the staff?

- 11.** We note in our major points above the widely acknowledged problems in this area: complex accounting issues and mathematical models used in valuations are compounded by a lack of available audit evidence and expertise. These issues are largely beyond the control of auditors but auditors can and should be encouraged, through auditing standards, to challenge management, third parties and specialists, more than they do now, on a number of different levels.
- 12.** We also note our belief that the outcome of this debate might be more effective if greater account were taken of a number of wider structural issues, including the competence of auditors and the resources available to them. Taking estimates and fair values at face value and simply seeking corroborative evidence to support management's assertions, without challenging them, is not acceptable. But dealing with a lack of auditor confidence, and a lack of ability or willingness to challenge, cannot be achieved simply by setting out in detail the questions auditors should ask and what they should do in any given set of circumstances. The people who develop and promote the complex estimates and fair values embedded in some financial instruments are highly qualified, highly paid and sophisticated. The models on which such instruments are based are often technically complex. An effective audit requires auditors with the experience, competence and time budgets to effectively challenge these bases of calculation. At present, auditors do not always have the necessary combination of qualities and resources. We urge the PCAOB to acknowledge and address these issues, where possible, in its deliberations.
- 13.** We do not believe that auditing standards need to address issues relating to national-level pricing desks. They are essentially issues of methodology and are not relevant to the development of auditing standards. The principles and requirements that should be applied by auditors using national-level pricing desks are the same as those that should be applied by auditors that do not.

Different possible approaches

Q4. Do accounting estimates and fair value measurements have sufficiently common attributes that the audit procedures should be included within a single standard? Are there limitations to the approach of having a single standard address both auditing accounting estimates and fair value measurements?

Q5. Are there considerations affecting accounting estimates relative to the financial reporting frameworks, such as recent changes to revenue recognition, that the staff should specifically take into account in developing a potential new standard?

Q6. Are there other considerations relating to the alternatives explored, including other alternatives not discussed in this paper, that the staff should consider in connection with this project?

Q7. Based on commenters' experience in applying ISA 540 (or AU-C 540), are there any aspects, positive or negative, of a single-standard approach that the staff should consider in connection within a potential new standard? Are there any other lessons learned from the implementation of ISA 540 (or AU-C 540) that the staff should consider in its approach to standard setting in this area?

Q8. If AU sec. 332 were to be superseded, are there elements that should be retained? With respect to derivatives and securities, are there enhancements related to auditing assertions other than valuation that the staff should consider?

Q9. Are there considerations relevant to auditing accounting estimates and fair value measurements including other regulatory requirements³⁷ specific to certain industries that the staff should take into account?

- 14.** We note in our major points above our full support for international harmonisation and the consolidation of audit requirements for estimates and fair values into a single standard. There are many similarities (as well as some important differences) between estimates and fair values and harmonisation is a worthy objective of benefit to US investors. The PCAOB should seek to build on the good work performed by IAASB in this area. It is, however, essential to recognise that IAASB's ability to bring estimates and fair values together was dependent on the framework within which its standards are developed. This is a principles-based framework with high-level requirements supported by non-mandatory application material. In this case, it is buttressed by a non-mandatory IAPN.
- 15.** ISA 540's success hangs on the distinction between high-level requirements and non-mandatory application material. This distinction does not exist in the PCAOB's standards and the overall impression given by this CP is that staff would like to develop mandatory requirements in areas that are currently non-mandatory within ISA 540 and IAPN 1000.
- 16.** We also note in our major points above the importance of auditor judgement, challenge and professional scepticism. Auditors need the competencies and resources to challenge management and third parties. Auditor resources include auditing standards that permit and encourage them to exercise judgement. The word 'challenge', in the context of challenging management, does not appear in the CP at all. The opportunity should be taken to reinforce the importance of challenge and scepticism and the PCAOB might consider using material from Staff Audit Alert Practice Alert No. 10 on professional scepticism in this context. Preparers and auditors should be encouraged to recognise their responsibilities for the development and audit respectively of estimates and fair values, especially where third parties are involved. These responsibilities cannot be outsourced or delegated.
- 17.** Many of the specific requirements proposed in the CP would be better expressed as guidance on how to apply the main principles, rather than as explicit requirements. Alternatively, requirements might be better expressed as requirements for auditors to consider whether the performance of a number of different procedures, from a list of possible procedures, is appropriate.
- 18.** Specific aspects of the audit of fair values peculiar to that area include the fact that the audit of fair values is more process-driven than the audit of other estimates. At the same time, developing and auditing fair values often involve a high-level of judgement and the expertise required to exercise it. The overall impression given by this CP is that the process requirements surrounding fair values are being imposed on estimates generally and that the PCAOB is adding to current requirements in an attempt to make sure that there is less scope for abuse. The overall effect of this is in terms of additional *requirements* raises the bar. But we are not convinced that the additional cost of all of this, ultimately borne by investors, will result in proportionately enhanced benefits. There is a real risk that the outcome will be ever-

lengthier checklists that will do little to improve the quality of accounting estimates or the audit thereof, or enhance auditor scepticism.

- 19.** Innovation in audit is desired by regulators and firms alike but it comes at a price. Innovation requires judgement and judgement always involves the risk of misjudgement. If the risk of misjudgement is to be avoided at all costs, there can be no innovation. The audit of estimates in general and fair values in particular, is a minefield. There will always be developments that regulators will not have considered when issuing standards. A principles-based standard with fewer but tougher requirements, and more non-mandatory guidance material, would more readily accommodate innovation.
- 20.** For these reasons, we do not support specific procedures to address particular standards, such as the new revenue recognition standard. Similarly, we do not believe that there are considerations specific to certain industries that staff should take into account. Specific procedures will be required for every industry development and every time a new standard is implemented. Auditors will simply default to whatever is mandated rather than using their professional judgement to develop the most appropriate procedures within the relevant framework.

Risk assessment

Q10. Should the requirements for identifying and assessing risks of material misstatement with respect to accounting estimates and fair value measurements – including risk assessment procedures – be included in Auditing Standard No. 12 or be separately set forth in a potential new standard on auditing accounting estimates?

Q11. Are there additions or revisions to the existing requirements in PCAOB standards for identifying and assessing risks of material misstatement regarding accounting estimates that should be considered?

- 21.** The specific risk assessment requirements and procedures associated with accounting estimates and fair value measurements should be included in AS No. 12.

Understanding processes

Q12. Is the potential amendment to Auditing Standard No. 12 described above clear and appropriate for both accounting estimates and fair value measurements? Are there other matters relevant to understanding the process used to develop accounting estimates or fair value measurements that could be included in Auditing Standard No. 12?

Q13. In circumstances where the company uses information obtained from a third party, are there matters— such as information systems at third parties, controls that management has over the work of third parties, and controls at third parties— not currently addressed in AU sec. 324, Service Organizations, or other standards that the staff should consider?

- 22.** The potential amendment to AS No. 12 described is appropriate and it might also refer to fair values.

- 23.** Where an entity uses third party information, auditors need to use their judgement regarding the extent of work needed on matters such as information systems at the third party, controls that management exercise over the work of third parties, and controls at third parties. ISA 402 *Audit considerations relating to entities using service organizations* and ISAE 3402 *Assurance reports on controls at a service organisation* are relevant but we strongly caution against taking non-mandatory guidance for these materials (and/or SAS 70) and turning them into requirements.

Determining significant risks

Q14. Is the potential amendment to Auditing Standard No. 12 described above clear and appropriate for both accounting estimates and fair value measurements? Are there other factors that would be relevant in the auditor's evaluation of the degree of complexity of

judgment in the recognition or measurement of an accounting estimate or fair value measurement (e.g., the use of a third party for the determination of a price)?

Q15. Are there additional factors specific to accounting estimates or fair value measurements that would be useful in identifying significant accounts and disclosures, or in determining significant risks that should be considered?

Q16. Are there certain types of accounting estimates or fair value measurements that should be presumed to be significant risks?

24. The potential amendment to AS No. 12 described is clear but it is not appropriate for the generality of accounting estimates.

25. We note in our major points above our belief that auditing standards should not set out presumptions regarding which risks are significant. We have consistently opposed presumptions such as these in auditing standards and while we work with those that exist, we do not believe that a case has yet been made for their positive impact on audit quality. Nevertheless, if the PCAOB decides that some specific guidance is needed regarding the identification of significant risks, we believe that a *rebuttable* presumption that certain risks are significant would be better. The onus would be on auditors to show that the risk is not significant and would mean that in cases in which the risk was not in fact significant, work would not be performed for compliance purposes only. Such work is not cost-free.

Responding to risks: additional substantive procedures and conformity with the applicable framework

Q17. Are there considerations particular to the timing and extent of these procedures (e.g., interim audit procedures), beyond the requirements of paragraphs 42–46 of Auditing Standard No. 13, that the staff should consider including in a potential new standard?

Q18. Is the potential amendment to Auditing Standard No. 13 described above helpful in emphasizing the auditor's consideration of the applicable accounting framework when auditing significant accounts and disclosures?

Q19. Should a potential new standard include specific audit procedures related to auditing disclosures of accounting estimates (e.g., disclosures on levels within the fair value hierarchy)?

26. The potential amendment to AS No. 13 described would be more helpful if the word 'considering' were used in the place of 'testing'.

27. We do not believe that specific audit procedures related to disclosures of accounting estimates would be helpful, particularly if they are linked to specific disclosure requirements, since they risk being outdated when disclosure requirements change. Principles-based standards that can accommodate changes in accounting standards are preferable. Guidance material in this area might be helpful, or a requirement to the effect that auditors should consider whether the performance of a number of different procedures, from a list of possible procedures, is appropriate in the circumstances.

Tests of controls

Q20. Given the existing requirements related to testing controls in Auditing Standard No. 13 (and Auditing Standard No. 5, as applicable), would specific requirements on testing internal controls over accounting estimates be useful (e.g., evaluation of design and operating effectiveness of key review controls over accounting estimates)?

28. We do not believe that specific requirements on testing internal controls over accounting estimates would be useful. However, guidance material in this area might be helpful, or a requirement to the effect that auditors should consider whether the performance of a number of different procedures, from a list of possible procedures, is appropriate in the circumstances.

Procedures relating to significant risks

Q21. Should a potential new standard include specific audit procedures that would be applicable when the auditor identifies and assesses a risk related to accounting estimates as a significant risk? If so, are there factors regarding measurement uncertainty or any other characteristics relevant to staff considerations of potential audit requirements?

29. We do not believe that a new standard should specify audit procedures applicable to risks assessed as significant. Many auditing standards include specific audit procedures applicable to risks assessed as significant but they almost always involve auditors *considering* the performance of a number of different procedures, from a list of possible procedures.

Substantive procedures

Q22. Are there specific factors that affect the auditor's selection of approaches related to testing accounting estimates? What considerations would be appropriate for the auditor to take into account when determining which approach (or combination of approaches) for testing accounting estimates should be selected?

Q23. Aside from testing management's process, developing an independent estimate, or reviewing subsequent events and transactions as further discussed, should a potential new standard allow for or require other approaches to testing accounting estimates? If so, what other approaches would be appropriate?

Q24. Are there certain types of accounting estimates for which substantive procedures other than those described in this paper would provide better audit evidence?

30. The auditor's selection of approaches related to testing accounting estimates is important. Where there is a choice between developing an independent estimate, reviewing subsequent events or performing work on management's process, the latter is often chosen. It might be helpful to suggest that this is not always the most appropriate approach and that a display of professional scepticism is demonstrated by challenge rather than simply seeking corroborative evidence.

31. When IAASB last revised ISA 540, it actively considered whether there were any 'other' general approaches to testing accounting estimates, but it did not find any workable alternatives. The three established approaches are broad, have stood the test of time, and we are not aware that they have acted as a brake on innovation. We do not see any great merit in allowing for alternatives in these circumstances.

32. There are for sure certain types of estimates for which substantive procedures other than those described might provide better audit evidence, but we do not believe that auditing standards can or should attempt to cover all eventualities in this level of detail.

Testing the company's process and evaluating the method used

Q25. Are there enhancements to the existing requirements for testing data used by management to develop the accounting estimate the staff should consider?

Q26. Are the potential requirements described above for evaluating whether the company's method used to develop accounting estimates appropriate for both accounting estimates and fair value measurements?

Q27. In circumstances where the financial reporting framework does not specify the use of a particular valuation method, is the consideration of methods accepted by the company's industry relevant? Are there other criteria that auditors could use to evaluate the appropriateness of the company's method used to develop accounting estimates?

33. The potential requirements described above for evaluating the appropriateness of the method used are appropriate for the generality of accounting estimates. For fair values, there will be certain cases in which it is not possible to evaluate whether the valuation method is accepted within the industry because the information necessary to ascertain the position and make the evaluation cannot be obtained by auditors.

- 34.** Where the reporting framework does not specify the use of a particular valuation method, considering methods accepted in the relevant industry is relevant, if that information is available to auditors.

Identifying significant assumptions

Q28. Would a requirement for the auditor to determine which assumptions used by management are significant assumptions present difficulties in practice? Should the staff consider a requirement for the auditor to identify assumptions not used by management, which might be important to the recognition or measurement of the accounting estimate?

Q29. Is the potential requirement suggested above clear and appropriate for both accounting estimates and fair value measurements? Are there other specific characteristics of significant assumptions that should be included?

- 35.** We note in our major points above, and in our answer to question 16, our belief that it is not helpful for auditors to presume that certain risks are significant. We believe that auditors should make this assessment. We note that if there has to be a presumption, a rebuttable presumption would be better. Determining which assumptions are significant is similarly a matter of judgement and we would much prefer that the proposed 'list of significant assumptions' were converted to a non-exhaustive 'list of factors that auditors may consider, if applicable, when determining whether an assumption is significant', similar to the list described in our answer to Q30 below.
- 36.** We are concerned that the list above may result in too many assumptions being identified as significant simply because they meet one of the characteristics list above, when in practice they may not have a material impact on the estimate or fair value measurement. In such circumstances it would not be effective for the auditor to be required to perform audit procedures on such assumptions. Item a. in the list above seems to be an overarching category, encompassing items b-f within it. In isolation, items b-f might all catch minor variations in assumptions.

Evaluating the reasonableness of significant assumptions

Q30. Are the suggested factors described above appropriate for evaluating the reasonableness of significant assumptions? Are there other factors the auditor should assess when evaluating the reasonableness of significant assumptions relevant to accounting estimates?

- 37.** The non-exhaustive, 'if applicable' list of suggested factors for evaluating the reasonableness of significant assumptions is similar to the list described in our answer to Q29 above. This is appropriate for principles-based standards. The factors described are appropriate. It would be better if the phrase 'should evaluate' were replaced with the phrase 'may consider'.

Management's use of a specialist

Q31. Is the potential requirement described above appropriate for all types of accounting estimates? Are there other considerations that should be taken into account in applying this requirement to accounting estimates?

- 38.** We note in our major points above the widely acknowledged problems with the independence of some specialists engaged by companies and other third party valuation sources. There are often simply too few to go around. Further problems with the availability of external evidence to support their valuations arise from their use of proprietary information or methodologies that they are unwilling to release to auditors. The proposals for auditors to look for evidence from other third party sources and evaluate whether a methodology is accepted in a particular industry are impractical in the all too common cases in which there are no other third party sources of information about bespoke products, or where any such sources are unwilling or unable to provide the relevant information. The proposals to treat valuations from specialists and other third parties as if they were generated by the company itself simply ignore these

issues. If these proposals are developed, we are concerned that they will create confusion by blurring the responsibilities of management and auditors, and that they will effectively require auditors to form judgements on the basis of non-existent or unobtainable evidence. A broad debate involving a number of stakeholders is needed regarding how such valuations should be audited.

- 39.** We therefore strongly disagree with the proposed requirement to treat valuations from specialists engaged by the entity as if they were generated by the company itself, for any type of estimate. It is inefficient, as well as a strange pretence. It is also inconsistent with the requirements of COSO 2013, which require management to understand how the valuation has been prepared in detail, in terms of input assumptions, data sources and methodologies, and to understand the specialist's competence and independence. It makes no sense at all for auditors to simply ignore this work. Auditors should instead be required to take full account of the degree of actual and perceived independence and objectivity of such specialists in determining the nature and extent of work that is required to evaluate the information they provide.

Data and assumptions produced by the company/third parties and used by the auditor in developing an independent estimate

Q32. Are the potential requirements described above for developing an independent estimate, including the potential requirements regarding testing data and assumptions, clear and appropriate for both accounting estimates and fair value measurements? Would these requirements present challenges for certain types of accounting estimates and fair value measurements?

Q33. Are there additional considerations that should be addressed with respect to information obtained by the auditor from a third-party source?

Q34. Are there factors that the staff should consider when developing potential audit requirements for testing the reliability and relevance of data independently derived by the auditor or obtained from other sources?

Q35. Are there other matters relevant to developing a range that a potential new standard could address (e.g., requiring a sensitivity analysis)?

- 40.** The requirements for developing an independent estimate are clear and appropriate for both accounting estimates and fair value measurements.

Subsequent events

Q36. Are the potential requirements described above for evaluating audit evidence from events or transactions that occur subsequent to the measurement date through the date of the auditor's report, appropriate for both accounting estimates and fair value measurements?

Q37. Are there additional factors that should be taken into consideration when evaluating the relevance of the audit evidence obtained from events or transactions that occur subsequent to the measurement date through the date of the auditor's report?

- 41.** There are certain areas of GAAP, such as ASC 740 relating to uncertain tax positions, which limit the extent to which subsequent events are relevant to the measurement of a position at the reporting date. While the phrase, 'relevant to the recorded accounting estimate' may have been intended to cover this situation, we believe it would be helpful to add a bullet relating to consideration of GAAP requirements regarding subsequent events.

Use of third parties

Q38. Would the potential requirements described above address procedures performed by audit firms that use a centralized testing approach? Would these requirements create issues in practice for smaller firms?

Q39. Should the potential new standard require the auditor to use a third party that is different from the third party used by management? Would such a requirement present challenges for certain types of accounting estimates and fair value measurements?

42. We note in our major points above our opposition to the proposed requirement to treat information provided by third-party sources used by the company as if it was produced by the company itself. This is not appropriate for any type of estimate. To treat information from such sources as if it was generated by the company itself is inefficient, as well as a strange pretence. It is also inconsistent with the requirements of COSO 2013, which require management to understand how the valuation has been prepared in detail, in terms of input assumptions, data sources and methodologies, and to understand the specialist's competence and independence. It makes no sense at all for auditors to simply ignore this work. Auditors should instead be required to take full account of the degree of actual and perceived independence and objectivity of such third parties in determining the nature and extent of work that is required to evaluate the information they provide.

Using evidence from third parties

Q40. Would the factors noted above help the auditor in evaluating the reliability and relevance of evidence obtained from third-party pricing sources? Are there other factors that are applicable in determining the reliability or relevance of evidence obtained from third-party pricing sources?

Q41. Are there other approaches to testing evidence obtained from third-party pricing sources that the staff should consider?

Q42. How could a potential new standard differentiate between a third-party pricing source and a specialist?

Q43. Would the potential requirement address the various methods used by third-party pricing sources for determining fair value measurements of financial instruments (e.g., use of consensus pricing and proprietary models)?

43. The factors noted would help auditors evaluate the reliability and relevance of evidence from third-party pricing sources, but not if they are mandatory requirements to be performed on every occasion.

44. There are likely to be other approaches which the PCAOB staff may consider, but attempting to cover all eventualities in this level of detail in auditing standards is inappropriate and, very likely, ineffective.

45. There is no need for a new standard to differentiate between a third-party pricing source and a specialist as the same principles apply to both when evaluating work performed by them.

Economic impacts

Q44. What are the likely economic impacts, including benefits and costs, of the potential alternatives discussed in this consultation paper? Are there any unintended consequences that might result from the alternatives?

Q45. As part of considering the need for change, the staff is reviewing academic literature, including identified papers that synthesize the academic literature.⁸² Is there ongoing research or other information that the staff should consider in evaluating the economic aspects of changes in standards for auditing accounting estimates and fair value measurements?

46. If a new standard follows the approach proposed, it is likely to significantly increase costs in some areas, particularly by effectively ignoring third party involvement. In our view any benefit of this will be limited. The proposals also appear to be pushing for more involvement of specialists in audits, which will also increase costs.