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Office of the Secretary
PCAOB
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Ref. PCAOB Rulemaking Docket Matter No. 026

I appreciate the opportunity to comment on "The Auditor's Assessment of and Response to Risk." The comments are based on my experiences as an auditing professor; as a member of auditing standards setting bodies, including volunteer service as a member of the IAASB; and as an occasional expert witness in private and SEC audit-related litigation. However, the comments reflect my personal views.

Overall, I congratulate the Board for considering updates to *Interim Standards* in order to be more in line with those of other standards setting bodies. Elimination of unnecessary differences (page 8) is worthy of the Board's effort. Multiple sets of standards impose cost burdens on accounting students (and their professors), practicing auditors, audit firms, and the PCAOB, as well as society that ultimately must pay the costs of multiple standards and any differences should be justified.

My comments focus on a few specific paragraphs regarding the concepts of the integrated audit and materiality that I believe are confusing and may reduce audit quality rather than providing clear guidance that will help auditors, protect investors, and further the public interest.

Page A3-3, para. 7: This paragraph states "In an integrated audit, the auditor's risk assessment procedures are the same for both the audit of internal control over financial reporting and the audit of financial statements." I believe that this statement is misleading because it implies that there is *no difference* in procedures for the two audits. As Abe Akresh (GAO) makes clear in a recent academic paper ("Using the audit risk model to opine on internal control," December 9, 2008) the internal control audit focuses on the *risk of failing to detect material weaknesses,* rather than the risk of failing to detect material misstatements.

For example, internal control audits require consideration of whether the auditor's *own procedures* for evaluating the design of internal controls might fail to detect a material design weakness, while tests of controls in financial audits facilitate assessment of control risk *per se* (see also, comment on page A4-6, para. 14 and 17). The two objectives are related but distinct, and because internal control audits are uniquely American, it is important for American standards to "get concepts right."

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Page A3-21, para. 56 : This paragraph should cross reference "tolerable misstatement" at the assertion level (see page A6-4, para. 8) to make clear that the risk assessment at the assertion level is based on an amount less than materiality for the financial statements as a whole. Otherwise, too little substantive auditing of each component might result.

Page A4-6, para. 14 and 17: These two paragraphs refer to a subtle difference between the objectives of internal control audits and financial statement audits with respect to Tests of Controls. One refers to a conclusion about whether controls are effective and the other to the auditor's control risk assessments (see comment on page A3-3, para. 7). It would be helpful to highlight and explain implications of the difference in objectives – perhaps as a Note.

Page A6-3, para. 3: The revision deletes explicit reference to the important and long standing concept of "quantitative" materiality, refers to the concept as "material based solely on qualitative factors," and demotes to a Note the warning about the auditor's inability to design practical (which I presume means cost effective) auditing procedures to detect quantitatively immaterial but qualitatively material misstatement. I assure you that the omission and demotion will cause much needless confusion to future auditing students because reference to this important limitation of auditing is indirect and thus obscure. Also, it will cause unnecessary discussion in preparation for audit litigation.

Page A6-4, para. 8: The first sentence is incomplete or misleading because it omits reference to the need to apply "tolerable misstatement" at the assertion, account balance, or class of transaction level when planning and performing audit procedures. One could read this paragraph as being applicable at the financial statement level rather than at a component level. A literal reading of present paragraph 8 would greatly *reduce* the amount of auditing traditionally applied, which is likely not the Board's intent.

I hope that the Board and its staff will find the above comments useful, and I would be pleased to discuss, elaborate, or answer questions about any points raised.

Sincerely,

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