



July 9, 2008

Mr. Arthur Levitt, Jr.
Mr. Don Nicolaisen
Advisory Committee on the Auditing Profession
Office of Financial Institutions Policy
Room 1418
Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

Comment Letter of The Value Alliance on the Draft Report and Report Addendum of the U.S. Treasury Advisory Committee on the Auditing Profession

Dear Mr. Levitt, Mr. Nicolaisen, and Distinguished Members of the Advisory Committee:

Thank you for the opportunity to comment on this important work of your Committee. I commend the Committee on its fine work and have comments related to two of the sections in the report.

Human Resources

There are five themes I'd like to address with respect to human resources.

- (1) Curricula and the way in which a profession is practiced can and do influence the make-up of those attracted to and those who remain in that profession. Updates to curricula are vital. In addition, there is also an ongoing need in the US to emphasize the quality of mind that auditors must possess, and in particular the need for auditors to possess the ability to exercise judgment in the midst of changing circumstances, including the proper exercise of broad, abstract, conceptual, and analytical thinking skills.
 - Mr. Wyatt in his speech "Accounting Professionalism – They Just Don't Get It" referenced in the Committee's bibliography states: "We must continue to emphasize the conceptual underpinnings to accounting".
 - The ICAEW's *Audit Quality* which is part of the Committee's bibliography outlines the issue this way: "Risks change over time. The external economic environment in which firms operate constantly change." (p. 12) "Auditors make judgments often in areas where there is no clear-cut answer provided in auditing and accounting standards, guidance, or precedent" (p. 13) and "The single most important audit technique is the application of sufficient thought at every stage. Most firms use standard audit approaches and documentation but a successful audit is not about mere box ticking. Instead auditors must use professional judgment to reach an appropriate audit opinion." (p.15, emphasis added)

To attract students and professionals who possess the quality of mind to perform excellent audits requires that curricula be designed around these core principles – in formal classroom and on the job training.

In my opinion, a profession cannot rely on *very specific* guidance from regulators and educators and hope to keep up with the pace of change in corporations. (The issues in the US financial services industry are recent examples of this.) Furthermore, as Ms. Minow stated in her testimony, in another context “an overly compliance-based approach suffocate[s] originality and eliminate[s] incentives for the development of optimal approaches for varying circumstances.”

In my opinion, some of the difficulties in implementation of Section 404 could have been lessened with a greater emphasis on broad based thinking skills and aptitudes -- and the challenges ahead with respect to fair value and IFRS (in addition to the fast paced change in the world economy and organizations themselves) will require a renewed effort to reinforce these core aptitudes, particularly vital for the leaders and educators of the profession. I believe if the US audit profession is not fully prepared with these capacities of mind, the transition to international, principle based and valuation based approaches will be a painful one, similar to what we witnessed in the implementation of 404.

On the ICAEW's website, ICAEW shares a quote from Caroline Stockmann ACA: “It is not difficult if you already have ACA training to then quickly learn the accounting standards of the different countries you are working in. It helps to assess quality of auditors, understand what Sarbanes Oxley requirements are about, and not be ‘thrown’ by anything technical, even if ‘new’.”

This seems to be an ideal our education should strive for.

Given the experience of other countries in implementing multiple standards and their approaches to education and certification which differ from the US model, I would recommend discussions with the ICAEW and others with an aim to review their approaches and assess their applicability as a means of facilitating a re-emphasis on core skills and aptitudes with respect to conceptual and analytical thinking. (I note that Recommendation 6 of the Committee's report in the section entitled *Concentration and Competition* discusses the importance of these cross-border discussions in a regulatory context.)

- (2) I would recommend caution in approaches that might create even greater separation among and between the disciplines of accounting, finance, valuation and economics. (I have been invited to witness this academic rivalry at forums in the past.) Auditors must understand the principles of these various disciplines and their integration and inter-connection. Understanding the economics of transactions, in addition to the rules of reporting, for example, is vitally important to making the judgments required of a good audit. All of these disciplines are important to auditors – and cross disciplinary analytical skills will increasingly be required. The Robert Half release of July 16, 2007 Financial Leasers Address Challenges Facing Accounting, Finance and Audit Professions, which is part of the Committee's bibliography discusses this stating: “As financial professionals assume more strategic roles, they will need to become more analytical. They must be able to not only produce financial reports and perform complex calculations, but also identify and explain what is meaningful in their data or findings. They need to be able to answer the “why” behind the numbers.” Auditors also must possess these skills.
- (3) Ethics is another area of importance as Mr. Wyatt's speech indicates. In talks I have given to auditor groups and in their follow up conversations with me, it is clear to me that there is a deep need to address the ethical questions faced by auditors (internal and external). One recommendation I would have is for an anonymous ethics hotline for the profession (perhaps similar to the one ICAEW offers) which auditors could call to discuss how to handle ethical situations that may arise in their firm and in their audits. This hotline might be an excellent way for professors on sabbatical to learn first- hand about some of the real world issues and pain facing auditors in the field.

- (4) Another important issue with respect to human resources is incentives. I believe audit firms should be encouraged to base compensation, promotions and other rewards first and foremost on the quality of audits they perform using robust approaches internally for assessing audit quality on individual projects, perhaps using the indicators that are developed in Recommendation 3 in the section entitled *Concentration and Competition*.
- (5) I agree with Ms. Gillan's testimony regarding the importance of women to the profession and the need to address the issues she outlines.

Firm Structure and Finances

The *Over-arching Principles of the Working Discussion Outline* state: "The quality of the audit process and audits is accomplished when the credibility of the audit meets the needs of investors" and increases when audits contribute to "investor confidence"..."transparency" and "lower the cost of capital". (emphasis added) I support those aims and therefore also support Ms. Minow's comments regarding the importance of auditors' work with respect to fraud detection since that work serves the overarching principles and aims by addressing the needs of investors, fostering investor confidence, increasing transparency and lowering the cost of capital. Based on my experience, I would note that clarification of the role of auditors in this regard is not only important for auditors and investors, but also, as a practical matter, for audit committees and boards in their oversight roles.

Thank you for the opportunity to comment. If you have any questions, I may be reached at 614-571-7020 or ebloxham@thevaluealliance.com.

Sincerely,

Eleanor Bloxham
CEO, The Value Alliance and Corporate Governance Alliance