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AICPA Peer Review Board
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(via email to PR_expdraft@aicpa.org)

EXPOSURE DRAFT: *PROPOSED REVISIONS TO THE AICPA STANDARDS FOR PERFORMING AND REPORTING ON PEER REVIEWS: Performing and Reporting on Peer Reviews of Quality Control Materials (QCM) and Continuing Professional Education (CPE) Programs* -- June 1, 2010

To the members of the AICPA Peer Review Board:

Thank you for the opportunity to submit comments on the above-referenced Exposure Draft ("ED"). I support the efforts of the Board to clarify the guidance for those involved in the development and maintenance of QCM or CPE programs. However, I have serious concerns about the proposals as they relate to QCM or CPE programs developed by third-party or commercial organizations.

My interest in the ED

I am a retired audit and national consulting partner of a Big 4 firm. Since retirement I have assisted accounting and audit standard setters in a variety of capacities.

My interest in the ED is several-fold. I recently completed four years as a public interest member of the Auditing Standards Board ("ASB") and continue as chair or member of several ASB task forces. Also, I participate in reviews of updates to an audit guide published by Thomson Reuters (formerly Practitioners Publishing Company ["PPC"]). I am not in active practice, and thus am not involved in any peer reviews.

My first exposure to commercial QCM was in connection with the Panel on Audit Effectiveness (the "Panel," also referred to as the O'Malley Panel). At the request of the SEC, the blue-ribbon Panel was commissioned by the Public Oversight Board to thoroughly examine the then-current audit model. I served on the Panel staff.

The Panel issued its report and recommendations on August 31, 2000 (http://www.pobauditpanel.org/download.html). Appendix K of the Panel report (a copy of which accompanies this letter) mentions that the Panel reviewed one commercial QCM

"… since these publications represent the core methodologies that a large number of smaller firms use."

The Panel was surprised to learn the extent to which the publications of PPC were used by smaller firms. Accordingly, as indicated in the Panel report, the Panel staff reviewed and analyzed those materials.

The Panel was impressed with the quality and professionalism of the PPC materials and the important role they play in audits by smaller firms. My later service on the ASB reinforced that importance. PPC (and others like it) serves as a surrogate national office for small firms, particularly as to audit methodologies and practice tools. As such, these QCM are a critical element of the quality of audits by small firms.

In 2005 PPC asked me to assist in the development of a new service, *PPC's Guide to PCAOB Audits.* My role has been to review and comment on portions of material prepared by PPC staff, principally on the SEC aspects of the audits of public entities.

Comments on the questions raised in the ED

First, let me acknowledge some confusion. The "Guide for Respondents" indicates that the questions are oriented to "the peer review relationships described in paragraph 159 of the *Standards*." However, paragraph 159 seems not to discuss "permitted relationships" but simply to list categories of developers of QCM or CPE materials, all in the context of peer reviews of those materials. (Also, the relationship of paragraph 159 to the cited interpretations seems indistinct.) Nonetheless, the broad context suggests that the Board is interested in reactions to proposed prohibitions on serving both as QCM/CPE developer and peer reviewer, and that inference governs my responses.

The questions and my responses seem interrelated. Therefore, I propose to respond to question 3 in the hope that I will have adequately responded to all the questions:

> *3. Do you believe that the proposed revisions are necessary to serve the main goal of the AICPA Peer Review Program (promoting quality in the accounting and auditing services provided by AICPA members and their CPA firms in order to serve the public interest and enhance the significance of AICPA membership)?*
>
> First, as to the conflict between development of QCM/CPE materials and peer reviews of users of those materials -- I believe that a "one-size-fits-all" approach to this issue is not in the public interest and may well result in either significant dilution of the quality of QCM/CPE materials or fewer qualified peer reviewers – or both.
>
> I believe that the answer to whether a party who participates in QCM/CPE materials can also serve as a user peer reviewer is an unequivocal "maybe." That is, it depends on facts and circumstances rather than an overall prohibition in all instances. That would appear consistent with the risk-based approach to analyzing independence matters in the *Conceptual Framework for AICPA Independence Standards* (ET Section 100-1).

At one extreme, if a firm develops QCM, it should not peer review another firm that uses the QCM as its primary reference source. In that case, the developing firm has an interest in the reviewed firm because of the pervasiveness of common audit methodologies.

However, I believe there is an opposite extreme. Individuals who participate only occasionally in the development or review of third-party QCM/CPE materials may well still qualify as peer reviewers of firms that use those materials. While the extent of an individual's participation can vary, my experience (and understanding) is that these individuals most often provide fatal-flaw reviews of the materials, but are seldom involved in preparation. The participation is not extensive and the fixed stipends are not material by any measure. Nonetheless, the fatal-flaw reviews are critical to the public interest and to the user firms without national office functions that rely on them.

The balanced recognition of extent of involvement and materiality seems well-rooted in other interpretations of paragraph 21 of the Standards, *viz.*, Interpretations 21-5 through 21-8. For example, Interpretation 21-8 states that Firm A is independent of Firm B even it Firm A occasionally consults with Firm B with respect to specific accounting, auditing, or financial reporting matters. Consistent with that interpretation, Firm A should be independent of Firm B if Firm B uses QCM in which a Firm A individual has only occasionally consulted with the developers. Therefore, I urge that the Board consider these other interpretations in determining which participants in the development of QCM materials may also serve as peer reviewers of user firms.

The point is that there must be a practicable way both to prevent serious conflicts yet allow for peer reviews of user firms by those who are only occasional participants in the development of third-party QCM/CPE materials. Can it help the profession or the public interest if the result is to force qualified third-party QCM participants to choose between QCM and peer reviews? I fear one will necessarily suffer.

In conclusion, I recommend that the Board reconsider the proposed prohibitions. At a minimum, I suggest that it not paint all participants in the development of QCM/CPE materials with the same brush. The profession and the public interest seem ill-served by a proposal that seems to insure either fewer qualified peer reviewers or a reduction in the quality and reliability of third-party QCM/CPE materials.

Having served on both AcSEC and the ASB, I appreciate the difficulties the Board faces in proposing these revisions, and I wish you well in your deliberations. If I can be of any assistance, please feel free to contact me at either (203) 869-1989 or gpfritz@aol.com.

Sincerely,

George P. Fritz, CPA