



AMERICAN ACADEMY
of ACTUARIES

February 22, 2008

International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, New York 10017 USA

Re: Proposed International Standard on Auditing (ISA) 620 (Revised and Redrafted), “Using the Work of an Auditor’s Expert”

The following are comments on the Proposed ISA 620 (Revised and Redrafted) by the American Academy of Actuaries’¹ Financial Reporting Committee. We thank you for the opportunity to comment on this proposed audit standard, especially given the role of actuaries in their work as outside experts for the auditing of insurance enterprises and the auditing of pension and retiree benefit estimates for nearly all enterprises.

The organization of this letter is: first; general comments then responses to the specific questions raised in the proposed revised audit standard; and finally, responses to individual paragraphs of that proposed audit standard.

GENERAL COMMENTS

With regard to accounting estimates based on the work of experts, we believe that the proposed audit standard should more thoroughly address the potential uncertainty surrounding such estimates. We believe that this is a major issue with regard to reliance on experts in areas containing significant uncertainty, whether the experts are those of management or the auditor.

Estimation uncertainty can sometimes lead different experts to arrive at materially different accounting estimates, each relying on their professional judgment. In such a situation, relying on a single point estimate from an expert without an understanding of the uncertainty in their estimate can lead to an inappropriate audit opinion (e.g., when the auditor’s expert and management make materially different estimates, but with both within a range of reasonable estimates allowed by the data and professional judgment). This is because the auditor may

¹ The American Academy of Actuaries is a national organization formed in 1965 to bring together, in a single entity, actuaries of all specializations within the United States. A major purpose of the Academy is to act as a public information organization for the profession. Academy committees, task forces and work groups regularly prepare testimony and provide information to Congress and senior federal policy-makers, comment on proposed federal and state regulations, and work closely with the National Association of Insurance Commissioners and state officials on issues related to insurance, pensions and other forms of risk financing. The Academy establishes qualification standards for the actuarial profession in the United States and supports two independent boards. The Actuarial Standards Board promulgates standards of practice for the profession, and the Actuarial Board for Counseling and Discipline helps to ensure high standards of professional conduct are met. The Academy also supports the Joint Committee for the Code of Professional Conduct, which develops standards of conduct for the U.S. actuarial profession.

sometimes erroneously view the difference as a misstatement rather than a sign of inherent (and potentially unavoidable) estimation uncertainty, worthy of disclosure rather than restatement.

With regard to the provisions in paragraph A4, whereby an auditor can effectively self-certify the auditor's (sufficient level of) expertise in an area other than auditing/accounting, we acknowledge that such a provision may be needed but note that it also raises additional risks. We recommend that the standard alert the auditor of the potential risk associated with evaluations outside the auditor's area of professional certification, with appropriate guidance on any steps to address such risk.

RESPONSES TO POSED QUESTIONS

- 1) Proposed movement of the use of management's experts to a different ISA.

Response: Although the proposed International Standard of Accounting (ISA) outlines several reasons for having separate standards working with management's expert versus the auditor's expert, there are several benefits to keeping the guidance on the use of experts in a single standard, rather than having separate standards for the use of management's expert versus the auditor's expert. As one example, consider the need to understand the uncertainty surrounding an expert's point estimate, as mentioned in our general comments. This issue exists whether the expert works for management or the auditor. In addition, the criteria for evaluating an expert's qualifications, professionalism and/or potential biases exist regardless of the expert's direct employer. There are several other areas where commonality of issues would require duplicating guidance, if the decision is made to have several separate standards dealing with the use of experts. These should be kept in mind when the IAASB makes its decision as to whether to have a single standard or multiple standards dealing with the use of experts.

- 2) Separation of the guidance regarding auditing and accounting experts from the guidance regarding experts in non-auditing/accounting areas

Response: We have no opinion as to whether the use of an expert for guidance in auditing/accounting areas should be separated from the use of an expert for guidance in non-auditing/accounting areas. However, we believe that the question worded in the proposed ISA 620 is slightly different. The question as worded excludes experts that have auditing/accounting expertise, whereas the definition of "expert" (paragraph) includes experts with expertise in areas *other than* accounting/auditing, not on whether such expertise is being used. This distinction is relevant where the expert has expertise in both auditing/accounting and non-auditing/accounting areas. The question as worded could be interpreted to scope out those providing non-auditing/accounting assistance if they also happened to possess auditing/accounting expertise; we do not believe this is the intent of paragraph 6.

COMMENTS ON SPECIFIC PARAGRAPHS

Paragraph 1

As worded, this paragraph and the following one do not clearly address the situation where an expert in a field *other than* auditing/accounting is also an expert in an area of auditing/accounting. We believe that this is inadvertent, and can be fixed by a slight rewording such as adding by ending Paragraph 1 with the phrase “to assist the auditor to obtain sufficient appropriate audit evidence *using such non-accounting/non-auditing expertise.*”

Paragraph 2

As a minor point, consistent with the concern raised with Paragraph 1 wording, we suggest a slight editorial change to Paragraph 2, so that it discusses “consultation with specialists *for* a particular area of accounting”, rather than the current “consultation with specialists *in* a particular area of accounting.” Otherwise, one interpretation is that it scopes out those experts with both specialized accounting expertise as well as non-auditing/accounting expertise, even where it is only the latter that is being relied upon by the auditor.

Paragraph 6a

Similar to the concern with Paragraph 1, this paragraph may need minor edits to address the situation where an expert in non-auditing/accounting areas is also an expert in auditing/accounting. Our suggested rewording follows (with the suggested change identified by italics). (In the definition of Expertise, include reference to Professional Judgment.)

“Expert – a person or organization, possessing expertise in a field other than accounting or auditing (*and where such non-accounting/auditing expertise is the basis of their engagement by the auditor.*)”

Paragraph 6b

We believe that the prudent application of professional judgment is a major component of an expert’s work. While we acknowledge brief mention of the role of judgment in paragraphs A9 and A14, we believe that it should have more prominence in the standard. One way to achieve this would be to make a slight change to the definition of “expertise” in this paragraph, so that it reads:

“Expertise – Skills, knowledge and experience *in the application of professional judgment* in a particular profession or specialized occupation.”

Paragraph 9

We agree with the objective criteria for the evaluation of an “expert” found in the accompanying paragraphs A10, A12-A13.

Paragraph 11

Use of an expert typically occurs in developing accounting estimates. Such accounting estimates can be subject to significant uncertainty, with potentially significant reliance on professional judgment. To the extent such reliance on judgment can lead to a range of reasonable estimates with material difference between the values within the range, we believe the auditor needs to obtain an understanding of the degree of uncertainty in the expert’s report. Where “the answer” is a matter of judgment within a broad range of possible reasonable answers, the auditor needs

more information than just a point estimate. We recommend that Paragraph 11 elaborate on this need.

The first sentence of this paragraph also appears to have a typographical error, which can be fixed by adding the word “on” after the second comma, so that it reads:

“The auditor shall agree, in writing when appropriate, *on* the following matters with the auditor’s expert:”

Paragraph 12

Auditors hire their own experts when they believe they do not have the internal resources to fully evaluate the matter under audit. As such, expecting the auditor to be able to fully “evaluate the adequacy of the auditor’s expert’s work” when such expert’s work is outside the auditor’s expertise does not seem reasonable. If the auditor were able to evaluate details such as “relevance and reasonableness” with regard to assumptions, methods and data, they are not likely to have retained their own expert. We suggest utilizing the more objective valuation criteria found in the current ISA 620, paragraph 14, which reads:

“The appropriateness and reasonableness of assumptions and methods used and their application are the responsibility of the expert. The auditor does not have the same expertise and, therefore, cannot always challenge the expert’s assumptions and methods. However, the auditor will need to obtain an understanding of the assumptions and methods used and to consider whether they are appropriate and reasonable, based on the auditor’s knowledge of the business and the results of other audit procedures.”

Paragraph A1

In order to provide greater visibility to the need for professional judgment (and unavoidable subjectivity) in many areas of expertise, we suggest the following editorial change to this paragraph:

“Expertise in a field other than accounting or auditing includes expertise in, *and the application of professional judgment to*, such matters as:”

Paragraph A4

This paragraph effectively allows an auditor to self-certify themselves with regard to non-accounting/auditing expertise. We acknowledge that an auditor will not always need to bring in an expert for such issues, but believe that such an option to self-certify sufficient expertise in an area outside the scope of ones professional certification raises additional risks. This is based on similar experience of professionals self-certifying themselves in areas outside their established area of expertise. Hence we recommend that additional guidance be added to this section addressing such increased risk.

Paragraph A5

We believe the important criteria of the present paragraph 7a “The engagement team’s knowledge and previous experience of the matter being considered” should be retained. We wonder why it was dropped.

Paragraph A25

We heartily endorse the reference concerning the need to communicate in A-25 which begins: “Effective two-way communication helps ...”. We believe the emphasis on effective two-way communication is important and deserves a place in the document. Perhaps A-25 or a shortened version thereof could be moved to a closing paragraph of 11 in the body of the standard.

Paragraph A29

At least some of our reviewers found this paragraph unclear. As a result, we offer this alternative version.

“When the auditor’s expert’s work relates to an accounting estimate developed by management, the auditor’s expert may be directed to evaluate the assumptions and methods (including models) underlying management’s estimate, or instead may be directed to develop an auditor’s point estimate or range for comparison with management’s point estimate. In the latter case, the assumptions and methods used by the auditor’s expert may be significant to the auditor’s use of that expert’s work.”

Once again, we appreciate the opportunity to provide comments on such a valuable standard, and one that will apply to many actuaries’ workproduct. We are available to respond to any questions you might have with regard to the above comments.

Sincerely,



Henry Siegel
Chairperson, Financial Reporting Committee
Risk Management and Financial Reporting Council
American Academy of Actuaries

The members of the drafting team that are responsible for this comment letter are as follows:



Ralph Blanchard
Member, Financial Reporting Committee
Vice Chairperson, Risk Management and Financial Reporting Council



Burton D. Jay
Member, Financial Reporting Committee



W.H. Odell
Member, Financial Reporting Committee

Kermitt Cox
Member, Financial Reporting Committee

James Verlautz
Member, Financial Reporting Committee