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2 August 2019

**Proposed Statement on Audit Standards, Amendments to the Description of the Concept of Materiality, and Proposed Statement on Standards for Attestation Engagements, Amendments to the Description of the Concept of Materiality**

Dear Ms. Hazel:

Ernst & Young LLP (EY) is pleased to submit this comment letter to the Auditing Standards Board (ASB or Board) in response to the ASB's request for comment on its proposed Statement on Auditing Standards (SAS), Amendments to the Description of the Concept of Materiality, and proposed Statement on Standards for Attestation Engagements (SSAE), Amendments to the Description of the Concept of Materiality.

We support the ASB's efforts to align the materiality concepts discussed in AICPA Professional Standards with the definition of materiality used by the US Supreme Court, the auditing standards of the Public Company Accounting Oversight Board, the Securities and Exchange Commission (SEC) and the Financial Accounting Standards Board (FASB). However, we do not support some aspects of the proposal and believe some proposed amendments require clarification. For example, as further explained in the Attachment, we believe that using the term "reasonable user" rather than "intended user," as the ASB has proposed, could confuse practitioners.

The Attachment includes our response to each of the ASB's questions in the Explanatory Memorandum as well as additional comments for your consideration. We would be pleased to discuss our comments with members of the ASB or its staff.

Sincerely,

*Ernst & Young LLP*

## Attachment – Comments on issues for consideration in the proposed SAS and proposed SSAE and other recommendations

### Issue 1: Revised definition of materiality

1. Please provide your views on whether the wording of the amendments is consistent with the definition of materiality used by the U.S. judicial system and other U.S. standard setters and regulators. If the wording is not consistent, please identify the areas of inconsistency and suggest alternate wording.

Overall, we support the ASB's proposal to change the description of the concept of materiality to be used as a frame of reference by auditors to determine materiality when planning and performing an audit of financial statements, if the applicable financial reporting framework does not include such a discussion about materiality. We believe that the proposed amendments are consistent with the definition of materiality used by the US Supreme Court and US standard setters and regulators. However, we believe the following changes to the ASB's proposed amendments would help clarify application of the concept of materiality and avoid unintended consequences.

#### *Proposed SAS, Amendments to the Description of the Concept of Materiality*

We believe the ASB should further clarify in any final SAS that the term "reasonable user," as described in the proposed amendments to paragraph .02 of AU-C Section 320, *Materiality in Planning and Performing an Audit*, refers to the same group of users as the current standard on materiality. However, this group of users isn't as broad as those referred to as "users" or "users of the financial statements" elsewhere in the auditing standards. To do this, we recommend that the ASB add the underlined words below to AU-C 320.04:

- .04 The auditor's determination of materiality is a matter of professional judgment and is affected by the auditor's perception of the financial information needs of users of the financial statements. When determining materiality for purposes of planning and performing the audit, the auditor should consider what would be material to reasonable users. In ~~the~~ is context of this section, ~~it is~~ the term reasonable ~~for the auditor to assume that users~~ refers to users of the financial statements that:
- a. have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;
  - b. understand that financial statements are prepared, presented, and audited to levels of materiality;
  - c. recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment, and the consideration of future events; and
  - d. make reasonable economic decisions on the basis of the information in the financial statements.

### ***Proposed SSAE, Amendments to the Description of the Concept of Materiality***

Overall, we support the amendments to AT-C Section 205, *Examination Engagements* and AT-C Section 210, *Review Engagements*. However, we are concerned that simply replacing the term “intended user” in AT-C 205.A17 and AT-C 210.A16 with “reasonable user” could be confusing and could have unintended consequences. Today, most practitioner reports issued under attestation standards are typically restricted use reports primarily because the criteria used to evaluate the subject matter are appropriate only for a limited number of parties or the criteria used to evaluate the subject matter are available only to specified parties. We believe use of the term “intended user” rather than “reasonable user” is more appropriate in the context of planning and performing an attestation engagement.

If the ASB replaces the term “intended user” with “reasonable user,” practitioners may infer that they should consider the needs of a broader range of users, other than those for whom the report was intended, when determining materiality. We recommend that any further changes to the concept of materiality in the Attestation Standards that may be necessary given the growing demand for general use reports should be addressed in the ASB’s separate proposal to revise SSAE No. 18.

#### **Issue 2: Consistency with current practice**

2. Please provide your views on whether the proposed amendments will change how auditors determine materiality in an audit or attestation engagement. If the amendments would result in a change, how would the change affect those engagements?

We wouldn’t expect the proposed amendments to significantly change our firm’s practices and guidance with respect to determining and applying materiality in an audit or attestation engagement. We observe that most financial statements audited in the US are prepared in accordance with US GAAP and that financial reporting framework already contains a similar concept of materiality, which auditors should use as a frame of reference when planning and performing the audit in accordance with AU-C 320.03.