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**Statement of William J. McDonough on PCAOB Conforming Amendments  
Related to Auditing Standard No. 2**

**September 15, 2004 Public Meeting of the Board**

Today's meeting is an important step in implementing Auditing Standard No. 2. That standard established a fundamental change in the way audits are conducted. Most significant, it articulated the concept of an integrated audit. An integrated audit combines an audit of internal control over financial reporting with the audit of the financial statements.

The examination of internal control helps the auditor better plan and conduct the audit of the financial statements and determine whether those statements are fairly presented. In this way, the integrated audit helps to achieve the Congress's intention to improve the quality and integrity of both corporate controls over financial reporting and of independent financial statement audits.

We adopted the integrated audit model in March this year, and we are now steaming toward full implementation, at least for the largest issuers, in November. We regularly hear from auditors and issuers about implementation matters. When we have become aware of broader practice issues, we have attempted to provide appropriate guidance. For example, Doug Carmichael and his staff issued a set of answers to frequently asked questions in June, and our staff will have more guidance shortly.

The proposal before the Board today is another part of our effort to make implementation proceed smoothly. This proposal would highlight for practitioners and other interested persons how AS 2 has affected the auditing standards that the profession developed and the Board adopted as its interim standards.

I emphasize that this proposal, and all the other things we are doing to make implementation easier, should not be misunderstood to replace the use of judgment in applying either the new internal control standard or the existing standards. Our goal in providing implementation guidance is not to create a detailed checklist for conducting an audit. Rather, our goal is to help practitioners and others better understand the principles underlying the standards and better appreciate why it's important that they use judgment in applying them.

We are committed to resolving appropriate issues in order to ensure a smooth transition, but we expect auditors and issuers alike to exercise judgment in applying the new standard in a manner that is appropriate given the context of the audit. For example, the standard does not require a one-size-fits-all audit program; rather, it provides auditors significant flexibility to tailor their audit programs to suit the size, complexity and nature of the public company subject to audit.

AS 2 is no different from any other auditing standard in that it does not prescribe detailed audit programs for specific sizes of companies. For as long as the profession has established auditing standards, auditors have used those standards to tailor their own audit plans, in a manner that addresses the nature and complexity of the audit client. The fact that the Sarbanes-Oxley Act did not

expressly establish classes of audit clients in no way limits the auditor's ability – indeed, responsibility – to use judgment to plan an audit that is appropriate to the circumstances. In the case of small companies, this should include the special considerations COSO outlines for internal control in such companies.

Finally, I want to thank Doug [and Tom Ray, who could not be with us today], and the entire staff of the Chief Auditor's office, for developing this proposal and for so ably shepherding AS 2 through implementation. This proposal reflects a tremendous amount of collective work by Doug, Tom, Laura Phillips, and Jennifer Rand. I would also like to commend the contribution Greg Fletcher has made to other aspects of the implementation effort. I am very pleased with the recommendation before us. Thank you for all the hard work.