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United States Government Accountability Office
Washington, DC 20548

May 12, 2008

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

Subject: PCAOB Rulemaking Docket Matter No. 025: PCAOB Release No. 2008-002,
*Proposed Auditing Standard – Engagement Quality Review and Conforming Amendment
to the Board's Interim Quality Control Standards*

This letter provides the U.S. Government Accountability Office's (GAO) comments on the Public Company Accounting Oversight Board's (PCAOB) proposed new auditing standard on Engagement Quality Review.

We appreciate the PCAOB's efforts to establish auditing standards on engagement quality review for registered companies and agree that this process is a critical element of an entity's quality control system. However, for reasons that we cite below, we believe that the public interest would be better served if the PCAOB adopted the engagement quality review standard included in proposed International Standard on Quality Control (ISQC) No. 1 (Redrafted), *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, or recently adopted Statement of Quality Control Standards (SQCS) No. 7, *A Firm's System of Quality Control*.

As we've stated in previous comment letters on proposed PCAOB standards, we strongly believe auditing standard setters should work together to achieve core auditing standards that are universally accepted. Where there is a clear and compelling reason, the individual standard-setting bodies should develop additional standards necessary to meet the needs of their respective constituencies. The nature of any differences from core auditing standards and the basis for the differences also should be communicated. For instance, GAO's *Government Auditing Standards* uses the same core field work and reporting standards as the AICPA's Auditing Standards Board (ASB) and supplements them with additional standards to satisfy the unique accountability needs of government entities.

The PCAOB has proposed a standard that diverges in overall approach as well as in certain details from ISQC No. 1 and SQCS No. 7, which were subject to due process and will be used by audit organizations globally. The PCAOB's decision to issue an engagement quality review standard that differs from these standards will create inconsistencies in core standards that may increase audit costs and lead to potential confusion and misapplication of the standards.

Instead of issuing a new standard on engagement quality review, we believe the PCAOB should amend its interim standards to incorporate the ISQC No. 1 or SQCS No. 7. Both standards include requirements and guidance on engagement quality review. By amending the interim standards, the PCAOB need only address any additional requirements or differences from the interim standards that the Board believes are necessary, thereby focusing auditor attention on the incremental differences between the PCAOB standard and those of the other standard-setting bodies.

Enclosure 1 to this letter contains our views on the specified questions in the release that accompanied the proposed auditing standard.

We thank you for considering our comments on this very important issue.

Sincerely yours,

A handwritten signature in black ink that reads "McCoy Williams". The signature is written in a cursive, flowing style.

McCoy Williams
Managing Director
Financial Management and Assurance

Enclosures

cc:

The Honorable Christopher Cox, Chairman
Securities and Exchange Commission

The Honorable Mark W. Olson, Chairman
Public Company Accounting Oversight Board

Mr. Harold Monk, Jr., Chair
Auditing Standards Board

**GAO's Response to Specific Questions in
PCAOB Rulemaking Docket Matter No. 025 and Other Related Comments**

Question 1: The proposed standard does not explicitly state an overall objective of an engagement quality review. Should this standard state such an objective? If so, what should be included in the objective?

ISQC No. 1 and SQCS No. 7 do not explicitly state an overall objective of an engagement quality review. However, such an objective could be developed based on the definition of engagement quality review in ISQC No. 1, paragraph 12(c) and SQCS No. 7, paragraph 5(d), such as the following:

The objective of an engagement quality review is to provide an unbiased evaluation, before the date of the report, of the engagement team's significant judgments and the conclusions they reached in formulating the report.

Question 2: Should an engagement quality review be required for all engagements performed in accordance with the standards of the PCAOB? If not, when should an engagement quality review be performed?

We agree that an engagement quality review and concurring approval of issuance should be required for audits of all registered companies. This is consistent with paragraph 41(a) of ISQC No. 1, which requires an engagement quality review for all audits of financial statements of listed entities.

Question 3: Are the qualifications of an engagement quality reviewer appropriately described in the proposed standard? If not, how should they be revised?

Paragraphs 46-48 and A42-A47 of ISQC No. 1 and paragraphs 92-98 of SQCS No. 7 include appropriate standards and guidelines on criteria for the eligibility of engagement quality control reviewers.

Question 4: Should the proposed standard allow the engagement team to consult with the engagement quality reviewer during the engagement? Would such consultation impair the reviewer's objectivity?

Paragraphs 46(b), 47-48, A43, and A44 of ISQC No. 1 and paragraphs 96-98 of SQCS No. 7 include appropriate standards and guidelines on the extent to which it may be appropriate for an engagement team to consult with the engagement quality reviewer during the engagement, as well as requirements and guidance to follow if the reviewer's objectivity becomes impaired.

Question 5. Are the descriptions of the scope and extent of engagement quality review procedures contained in the proposed standard appropriate? If not, how should they be changed?

Question 6. Is the risk-based approach to the engagement quality review described by the proposed standard sufficient to identify significant engagement problems? If not, how should the proposed standard be changed?

We support adopting a risk-based approach to the engagement quality review process and believe that any new audit standards should balance the desire to improve audit quality and value against the danger of becoming overly prescriptive.

The principles-based approach in proposed ISQC No. 1, paragraphs 43-45, A38 and A40, and in SQCS No. 7, paragraphs 85-91, broadly describe the nature, timing, and extent of the engagement quality control review procedures. Both of these standards allow the reviewer to identify documents for review based on audit risk and the nature of the engagement.

Question 7: Are the proposed requirements for the review of the engagement team's documentation appropriate? If not, how should they be changed?

Paragraphs 44-45, A38, and A41 of ISQC No. 1 and paragraphs 87-88 of SQCS No. 7 include appropriate standards and guidance for the review of the engagement team's documentation.

Question 8: Is the description of the timing of the engagement quality review, as proposed, appropriate? If not, how should it be changed?

Paragraphs A39 of ISQC No. 1 and paragraph 90 of SQCS No. 7 provide appropriate guidance on the importance of conducting the engagement quality control review in a timely manner at appropriate stages during the engagement.

Question 9: Is the standard for the engagement quality reviewer's concurring approval of issuance appropriate? If not, how should it be changed?

We support the provisions of SQCS No. 7, paragraph 81, which requires "...that the [engagement quality control] review be completed before the report is released." Statement of Auditing Standard No. 103, *Audit Documentation*, defines the report release date as "the date the auditor grants the entity permission to use the auditor's report in connection with the financial statements." Alternatively, ISQC No. 1, paragraph 49(b) requires the engagement quality control to be "completed before the date of the [auditor's] report."

Question 10: Are the documentation requirements for an engagement quality review appropriate? If not, how should they be changed?

Question 12: Should the proposed standard require documentation of the engagement quality review to comply with other provisions contained in AS No. 3? If so, which provisions should be applicable?

We support the provisions of paragraph 99 of SQCS No. 7, which requires firms to establish documentation policies and procedures for engagement quality control reviews, “including documentation that

- a. The procedures required by the firm’s policies on engagement quality control review have been performed;
- b. The engagement quality control review has been completed before the report is released; and
- c. The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions they reached were not appropriate.”

The documentation requirement in ISQC No. 1, paragraph 49 is essentially the same as SQCS No. 7 except for the provision for documentation policies and procedures to require that “the engagement quality control review has been completed before the date of the [auditor’s] report.”