

FEBRUARY 26, 2008 OPEN MEETING

PROPOSED AUDITING STANDARD ON ENGAGEMENT QUALITY REVIEW

Statement of Chairman Mark W. Olson

Thank you, Mr. Niemeier and Mr. Gradison.

The question before the Board today is whether it should propose a new auditing standard on engagement quality review and a conforming amendment to the Board's interim quality control standards

Section 103 of the Sarbanes-Oxley Act of 2002 mandated that the PCAOB adopt a requirement that each registered public accounting firm provide a concurring or second partner review and approval of each audit report, and concurring approval in its issuance, by a qualified person associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer.

Understanding the tangible enhancement to audit quality that a well-performed engagement quality review can provide, the PCAOB invested time and resources to examine thoroughly the existing requirements and current practices. To do so, the PCAOB used a number of the tools available to it, including its inspection and enforcement experience and discussions with its Standing Advisory Group. Based on this input, the Board concluded that it could further improve the second partner review process. The proposed standard that the professional staff brings to the Board today is the result of this careful work.

Importantly, due to the global environment in which the PCAOB and auditors operate, Tom Ray and his team also evaluated the current requirements in IAASB standards (namely Proposed Redrafted International Standard on Auditing ("ISA") 220, *Quality Control for an Audit of Financial Statements*, and Proposed Redrafted International Standard on Quality Control ("ISQC") 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*). Many of the provisions within the proposal align with these proposed IAASB standards.

I thank Tom Ray, Greg Scates and their colleagues in the Office of the Chief Auditor for their hard work on this proposal. I also thank the staff in the Division of Inspections and Registration and the Division of Enforcement who collaborated with our standards team by providing insights on current practices and short-comings that could

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be addressed in a new standard. The PCAOB's standard setting truly benefits from this type of cross-pollination.

To encourage improved practices, the PCAOB shares insights it obtains through its inspections program. For example, last October, it included observations related to concurring partner reviews in a report on certain findings from the 2006 inspections of smaller firms. The report reminded firms that they should ensure they are allocating appropriate resources to the performance of effective concurring partner reviews, and of the need to conduct the review with objectivity and due care. The PCAOB stressed in the report that firms also need to ensure that they are selecting competent reviewers to perform the concurring partner reviews and, if necessary, that a firm should consider engaging as the concurring partner an accountant who is not affiliated with the firm if the firm does not have a qualified individual with the appropriate level of expertise and experience to perform an effective review. The observations described in the October report influenced the proposal that the Board is considering today.

As Tom Ray and Greg Scates have just described, the proposed standard and conforming amendment would take a risk-based approach to the engagement quality review. The proposed standard builds on the strengths of the Board's interim requirement and the best practices of the profession. It would provide for a more explicit focus on identifying and reviewing those areas in the engagement likely to contain higher risk. After performing certain specified procedures, the reviewer would be required to assess whether there are areas within the engagement that pose a higher risk that the engagement team (1) failed to obtain sufficient competent evidence or (2) reached an inappropriate conclusion. In these higher risk areas, the engagement quality reviewer would be required to evaluate whether the engagement team responded appropriately to the assessed risks, the judgments made were reasonable, and the results of the procedures performed support the engagement team's overall conclusion. Due to the high value that the PCAOB places on the benefits of an engagement quality review, the proposal expands the current requirement to cover all engagements conducted in accordance with PCAOB standards.

I understand that many firms – beyond those that are currently required to do so - have procedures for concurring procedures substantially in place, and for them, as proposed, such firms would likely only need to modify their procedures. Firms that were not members of the SEC Practice Section and who do not already voluntarily perform a concurring partner review will need to invest resources to build an effective review in

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accordance with the new standard. The proposal provides flexibility for smaller firms by, among other things, allowing them to work with qualified individuals outside of their own firm to perform the required review. The reviews themselves are envisioned as being risk-based; this reflects the view that it is possible to increase the likelihood of identifying and correcting deficiencies in an audit prior to issuing the audit report, in an efficient manner.

As with all standards-setting initiatives, proposed standards benefit from public input. I therefore encourage stakeholders to review this proposal and provide their insights on how it could be improved. We will, as always, carefully consider all comments received. We have seen that engagement quality reviews are an important element of assuring high quality audits. I support this proposal and encourage comments to contribute to this important standard setting initiative.

I will now turn to my fellow Board members for any discussion.